ACQUISITION ADVISORY PANEL
Meeting Minutes
July 27, 2005
The Hyatt Regency Hotel
Long Beach, CA

The Acquisition Advisory Panel (AAP) convened its ninth meeting on July 27, 2005 in the Beacon B Room of the Hyatt Regency Hotel, 200 South Pine Avenue, Long Beach, CA. Ms. Marcia Madsen, Chair of the Acquisition Advisory Panel, opened the meeting at approximately 09:05 A.M.

The Chair welcomed everyone and thanked the Panel members in attendance for taking the time to journey to the West Coast. She provided information on the next Panel meeting scheduled for August 18th at FDIC in Washington. That meeting will include panels on Time & Material (T&M) contracting and Commercial Practices. Ms. Madsen also provided information on Capitol Hill activity of interest to the Panel including that the Senate is holding a series of procurement oversight hearings, the first of which occurred July 26th where the Administrator of the Office of Federal Procurement Policy (OFPP) referenced the work of the AAP. Ms. Madsen stated that the prospects continue to be good that the Panel's tenure will be extended, but that with other pressing Congressional activity, the bill would likely not be passed before October; therefore, Panel activity needs to continue on its current timeline.

Ms. Laura Auletta, the AAP's Designated Federal Officer (DFO), called the roll. The following Panel members were present:

Mr. Frank J. Anderson
Mr. Carl DeMaio
Mr. Marshall J. Doke, Jr.
Mr. Jonathan Lewis Etherton
Mr. James A. (Ty) Hughes, Jr.
Ms. Marcia G. Madsen
Mr. Roger D. Waldron
Mr. David Javdan

The following Panel members were not in attendance:

Mr. Louis M. Addeo
Dr. Allan V. Burman
Mr. David A. Drabkin
Ms. Deidre A. Lee
Mr. Tom Luedtke
Mr. Joshua I. Schwartz

The following is a summary of guest speakers and their affiliations:

Presenter	Affiliation	Acronym (If applicable)	Attachment
Mr. Neal Couture	National Contract Management Association	NCMA	Attachment 1
Ms. Ellen Polen	Space & Naval Warfare Systems Command	SPAWAR	Attachment 2
Mr. Michael Clancy	Oracle Corporation		Attachment 3
Mr. Matt T. Verhulst	Federal Supply Service, General Services Administration	FSS/GSA	Attachment 4
Mr. Robert S. Ayers	Science Applications International Corporation	SAIC	Attachments 5 & 6
Mr. John Young	Northrop Grumman Corporation		Attachment 7
Mr. Blaine Manson	Naval Air Warfare Center Weapons Division (NAWCWD), China Lake		No Material
Mr. Richard Hollis	Hollis-Eden Pharmaceuticals		Attachment 8

Panel Chair Marcia Madsen introduced the first presenter, Mr. Neal Couture, Executive Director of the National Contract Management Association (NCMA). In his prepared statement (Attachment 1), Mr. Couture thanked the Panel on behalf of the 17,500 members of NCMA for the opportunity to speak. He explained that NCMA is a neutral, non-lobbying organization that seeks to promote improvements in the public procurement process, and provide a forum for Government and industry. The focus of Mr. Couture's remarks was on workforce challenges facing the Federal Government. Specifically, he said that the size of the workforce has decreased concurrent with increases in both the volume and complexity of the workload. Mr. Couture believes that gaps in employee competencies exist, especially with respect to performance-based acquisition, best value source selection, general business expertise and adoption of appropriate commercial practices. Increasingly, he noted, there is *"relentless competition"* among agencies for the limited pool of experienced journeyman contracting officers, specialists and administrators. He sees an analogous situation in the private sector workforce. He expressed his concern on the need to attract talented entry-level personnel to the acquisition field in order to prepare for future succession of personnel into more senior positions.

Mr. Couture explained that NCMA is working to address workforce issues. These efforts include revising its "*Contract Management Body of Knowledge*" to include commercial practices competencies, expanding NCMA educational offerings, preparing a publication on performance-based acquisition, restructuring and expanding NCMA certification programs, and creating a university outreach program with strategies to attract entry-level talent to the field of acquisition. He suggested that the Panel recommend adoption of appropriate professional industry credentials as a substitute for some or all training and educational mandates required for service in Federal procurement positions that would allow contracting professionals from outside of the Federal Government to effectively compete for acquisition vacancies. Mr. Couture noted that that NCMA believes that similar barriers exist for other acquisition fields and that like measures to formally adopt equivalency policies should apply equally to these fields.

Mr. Couture opened the floor to questions from Panel members. In response to a question from Panel Member Carl DeMaio, Mr. Couture explained that NCMA's certification program is no longer hierarchical or peer-based because this methodology did not allow for accreditation.

Instead, NCMA's program now covers the entire spectrum of functions that should be mastered by a journeyman contracting professional. Panel Member Jonathan Etherton asked Mr. Couture if legislative or regulatory barriers exist that preclude adoption of the proposed NCMA equivalency model, and if new laws or policies should be established to further their proposal. Mr. Etherton explained that even when administrative authority to implement changes exists, incorporating specific legislative verbiage sends a clear signal of the direction Congress wishes to move. Mr. Couture said that the biggest barrier is cultural and a perception that it's "*just too hard*" to adopt new hiring practices. He said that even if new legislation were passed, he questioned whether it would be adopted at the local level.

Noting that he believes NCMA is uniquely qualified, Panel Member Marshall Doke requested that Mr. Couture solicit NCMA chapters for recommendations on improvements to acquisition processes. Mr. Couture replied that with the exception of the workforce issue, NCMA does not make acquisition policy recommendations; however, he agreed to pass on to the Panel comments that the NCMA membership has made on issues of interest. Panel Chair Marcia Madsen suggested that NCMA members respond to questions posted on the Panel's website, and that members engage with the Panel's established working groups.

In response to a question on adoption of commercial practices, Mr. Couture observed that businesses are realizing the importance of better management of existing business relationships and formalizing contracting processes. He said public companies are very interested in the Federal Government's acquisition model for acquiring goods and services, especially in light of transparency required by Sarbanes-Oxley. Mr. Couture explained that while different terminology is used by the Government and the private sector, acquisition approaches are becoming more similar, particularly with the increasing emphasis on the contracting professional *"being a business manager as opposed to a transaction processor."* Mr. Couture expressed his personal opinion that looking at the commercial world for solutions to Federal acquisition problems may not be fruitful because Government and the private sector have similar issues and challenges.

Panel Chair Marcia Madsen asked Mr. Couture for his perspective on non-traditional Government contracting shops such as Federal Systems Integration & Management Center (FEDSIM) and the Franchise Funds. Mr. Couture replied that business process outsourcing by commercial businesses is similar and that Professor Schooner wrote a paper on the marketing of contracting support services. Mr. Couture observed that using the non-traditional contracting shop, with its emphasis on selling its services to stay in business, may emphasize contract award over effective monitoring of contract performance. Ms. Madsen thanked Mr. Couture for his presentation to the Panel.

Panel Chair Marcia Madsen next introduced Ms. Ellen Polen, who as Corporate Contract Branch Head for the Space and Naval Warfare Systems Command (SPAWAR) is the lead for SPAWAR Headquarters' (HQ) implementation of the Navy's Sea-Port-Enhanced ("Sea-Port-E") contract. Ms. Polen began her presentation by providing an overview of SPAWAR's mission and organizational structure (Attachment 2). She discussed major contracting initiatives, highlighting SPAWAR HQ's success in the area of performance-based service acquisitions (PBSA); 74% of awards (calculated by dollars) are PBSA, significantly higher than Office of

Management and Budget's (OMB) goal of 40%. Ms. Polen discussed the Navy's virtual SysCom initiative, Sea-Port-E, noting that of the 492 indefinite delivery/indefinite quantity (IDIQ) contracts, 364 had been awarded to small businesses. She explained that a customer outreach program and use of a web-based e-commerce tool that provides policies, procedures and templates, contributed to the PBSA and small business achievements. Ms. Polen concluded her presentation with a policy recommendation to align and assign the approval level/threshold for information technology (IT) and non-IT acquisitions under $500M to the Program Executive Office (PEO), Head of the Contracting Activity (HCA), and Navy Contracting ("02").

Panel Member Carl DeMaio commended Ms. Polen on SPAWAR HQ's small business success and asked if the organization has an outreach program to enhance and grow small business capabilities. Ms. Polen replied that SPAWAR leadership and contracting officers are very supportive of small business and first look to small business to satisfy requirements. In response to Mr. DeMaio's comment that he hears complaints that working with small business increases costs to the taxpayer, Ms. Polen agreed - cost-type contracts with small businesses cost more because small businesses must build infrastructure. Often a small business must procure technical expertise at higher labor rates and small businesses need more attention during performance because of lack of familiarity with Government rules and procedures.

In response to a request from Panel Member Marshall Doke for more information on her organization's contract process management guide, Ms. Polen explained that this web-based interactive guide is available to the public and has sections on solicitation, evaluation, award and post-award phases of acquisition.

Panel Member Ty Hughes asked Ms. Polen to discuss in more detail SPAWAR HQ's approach to PBSA. She explained that the organization provided organic PBSA training, but then competitively selected a support contractor with PBSA expertise who conducted training and assisted program offices with translating requirements into performance-based statements of objectives and developing performance criteria and incentives. She stated that all performance-based task order requirements are maintained on-line, and are available as templates for all customers.

In response to questions from Panel Member David Javdan, Ms. Polen stated that SPAWAR HQ's 34% small business accomplishment is measured in dollars and captures activity at the prime contract only. In response to a question from Panel Member Roger Waldron regarding competing task orders among contract holders, Ms. Polen said that the program management function is multiple unrestricted awards to large businesses. She explained that for engineering, logistics, installation, test & evaluation (ELITE) contracts, where the list of seven contract holders includes four 8(a) contractors, there are no set-asides; each of the task orders is competed unless the situation satisfies a fair opportunity exemption. She added that for each instance where an 8(a) firm successfully competes for a task order, SPAWAR HQ counts the award in 8(a) metrics. A discussion ensued regarding whether an agency can take 8(a) credit when the competition includes non-8(a) firms.

In response to questions from Panel Members Marcia Madsen and Roger Waldron on the details of the IDIQ contract acquisition planning process that resulted in over 500 Navy Sea-Port-E

contracts, Ms. Polen explained that because the process was managed by the Naval Sea Systems Command (NAVSEA), she did not have the details; however, she provided her general understanding. The contracts were awarded to be "*the Navy's answer to multiple award contracts for services in the engineering field.*" Each contract has a nominal minimum order quantity of $2,500 to ensure each is a legal binding contract. Because only one solicitation has been issued, she could not speculate what the response from contract holders will be in terms of task order proposal submission. No fair opportunity exemptions will be permitted; valid sole source requirements will be accomplished under a separate contract with the vendor.

Panel Member Jonathan Etherton asked Ms. Polen what considerations had been involved in the Navy's strategy to establish its own multiple award contracts rather than using existing Navy or other organizations' vehicles. Ms. Polen said she could not speak for NAVSEA, but added that when establishing their own Major Service Acquisition (MSA) contracts, SPAWAR wanted more competition for better pricing, and longer-term relationships for better service from its vendors. Panel Member Frank Anderson asked if Navy customers are required to use Sea-Port-E. She replied that, while Sea-Port-E use is mandatory, with appropriate approvals, a fair opportunity waiver may be approved.

Panel Member Roger Waldron asked if SPAWAR had calculated and compared the savings derived from efficiencies gained by utilizing PBSA acquisition strategy. Ms. Polen said that while she did not know if the PBSA savings metric has been captured, corporate savings from the MSA program are estimated to be between 4 and 5%.

In response to questions from Panel Chair Marcia Madsen and Member Frank Anderson, Ms. Polen explained that the SPAWAR contracts are for support services and contain broad overarching statements of work under which each task order is competed. Mr. Anderson asked for a breakout of task orders that require "people-time" and those that are for pure taskings. Ms. Polen said that because of the complexity of the task orders, providing the breakout would be very difficult, but she agreed to provide representative samples of task orders.

Panel Chair Marcia Madsen asked Ms. Polen to discuss the reasoning behind the Navy award of such a large number (492) of Sea-Port-E IDIQ contracts. Ms. Polen explained that there were 492 local Zone 6 contractors interested in providing service, but that SPAWAR does not yet know how many offers they would receive for each order. The process includes issuing a solicitation on the internet, to which offerors will have the opportunity to respond with proposals that include technical, cost and sometimes management volumes. SPAWAR will then make best value award decisions.

Panel Chair Marcia Madsen thanked Ms. Polen for her time and effort in supporting the Panel.

Following her introduction of the next Panel speaker, Mr. Michael Clancy, Chief Counsel, Government Sector and Compliance of Oracle Corporation (Attachment 3), Panel Chair Marcia Madsen recused herself from the meeting, leaving the room, because Oracle is a client of her firm. Mr. Clancy provided a short overview of Oracle Corporation and its software and services businesses. He explained that Oracle is a software and services business comprised of 50,000 employees worldwide with 260,000 total customers including commercial companies of all sizes,

Government entities, educational institutions and resellers. The focus of Mr. Clancy's presentation was on commercial versus Government contracting practices. He explained that the biggest disconnect between Government and commercial IT software and consulting services involve T&M contract vehicles. For commercial IT services, T&M is the standard; per regulation, for Government contracting, a T&M approach is discouraged. Mr. Clancy made several recommendations associated with T&M vehicles including expanding the definition of commercial items to clearly and distinctly allow T&M contracts for consulting services, eliminating the restriction that T&M be used only if a Determination & Finding (D&F) stipulating that no other contract type is suitable has been executed, and, expanding FAR Part 12 to include specific subparts to separately address commercial services and consulting services as opposed to products.

Mr. Clancy compared a number of Government and Standard Commercial Terms in the areas of warranty, limitation of liability, audit rights, prepayment, and most-favored customer. He proposed specific recommendations including providing express authority for prepayment of software support services, development of audit provision revisions to allow for review of invoices at a commercially reasonable time, amendment of the FAR to adopt commercial remedies for implied warranties to avoid having to price risk, and adoption of commercial data rights terms for consulting services. Mr. Clancy also discussed the difficulty software companies have with providing subcontracting opportunities to small businesses because of the nature of the service software companies provide including supporting proprietary products. He suggested that agency small business goals should be tailored to the product, technology or system being procured.

Panel Member Marshall Doke thanked Mr. Clancy for his presentation, and asked if Oracle's commercial customers allow personnel substitutions. Mr. Clancy replied that typically, Oracle proposes a labor category, not a named individual; however, in some instances a name is provided and, with reasonable customer consent, Oracle may change personnel.

Noting that some large sellers segment their Government market from their commercial market, which can lead to difficulty in determining fair pricing, Panel Member Ty Hughes asked Mr. Clancy to discuss how Oracle sets a fair price in a non-competitive environment. Mr. Clancy explained that Oracle has a single commercial price list and that General Services Administration (GSA) reviewed Oracle commercial deals by labor category when establishing negotiated discounted schedule rates. He added that schedule pricing therefore benefits from the competitive commercial pricing. Mr. Hughes noted that the level of insight into Oracle deals that Mr. Clancy had described is not common for IT service providers. Mr. Clancy explained that the GSA process for establishing schedule prices is also based on disclosure of non-standard commercial situations.

In response to a question on small business opportunities from Panel Member David Javdan, Mr. Clancy reiterated that Oracle has very limited subcontracting opportunities, but agreed to research the issue to verify. Mr. Javdan asked if Oracle participates in programs such as Mentor-Protégé wherein large businesses work to educate small businesses. Mr. Clancy replied that he is not aware that Oracle participates in the program.

Panel Member Roger Waldron asked Mr. Clancy to elaborate on his recommendation that Government adopt the commercial practice of prepaying for software and its impact on pricing. Mr. Clancy said that Government administrative costs would be reduced, likening prepayment to a service subscription, and added that he would look into seeing if there are specific cost savings that might accrue. Mr. Waldron asked Mr. Clancy to elaborate on a previously stated objection to inclusion of a price reduction clause. Mr. Clancy explained that the complexity of IT services, including dependence for pricing on changing metrics, make implementation difficult, and noted that, ultimately, pricing in the software industry is driven by competition. He suggested that better pricing is achieved through acquisition strategies such as blanket purchase agreements (BPAs) off of schedules than price reduction clauses. Panel Chair Marcia Madsen thanked Mr. Clancy for his presentation.

Panel Chair Marcia Madsen introduced Mr. Matt Verhulst, Director, Contracts Division, Small Business Governmentwide Acquisition Center, of GSA's Federal Supply Service, Kansas City. Mr. Verhulst's presentation (Attachment 4) provided an overview of Governmentwide Acquisition Contracts (GWACs) and particulars on GWAC acquisition centers and the GWACs they administer. He defined a GWAC as a task or delivery order contract for information technology that is usually a multiple award contract established by one agency for Governmentwide use. GSA's GWACs are administered through three centers: Enterprise, Small Business, and Greater Southwest. Mr. Verhulst discussed the benefits of using a GWAC over other approaches including ease of use, flexibility, FAR compliance, limitations on the grounds for protest in accordance with Clinger-Cohen, and direct ordering availability. He explained that as an OMB-designated executive agent for a service contract, his organization reviews each task or delivery order for scope, fit, competition, and acceptability and that his organization has embraced the GSA "*Get It Right*" campaign. Additionally, Mr. Verhulst provided details on the various GWACs set-aside for small and small and disadvantaged businesses.

In response to questions from Panel Members Frank Anderson and Marshall Doke, Mr. Verhulst elaborated on the training program for GWACs. He explained that the training is very hands-on and geared to the warranted contracting officer. It addresses in detail fair opportunity in accordance with FAR 16.505, and preferences for fixed price orders with performance-based requirements. Mr. Verhulst agreed to provide training materials on fair opportunity including circumstances when it is appropriate to use exceptions.

Panel Member Jonathan Etherton asked Mr. Verhulst to discuss the clarity of roles and responsibilities of the agency contracting officer and GWAC contract holder. Mr. Verhulst stated that the roles are expressly articulated in a contracting officer delegation of authority, and he offered to provide a copy of a delegation to the Panel. Panel Members Jonathan Etherton and Roger Waldron asked whether GWACs are established to allow for new technologies to be incorporated. Mr. Verhulst explained that his organization looks at innovative trends and, when possible, builds them into solicitations and resulting contracts. Additionally, they include a provision that allows for an open season in which to add GWAC contractors.

Panel Chair Marcia Madsen asked Mr. Verhulst who assumes the responsibility for dealing with performance disagreements on task or delivery orders. Mr. Verhulst explained that management of the task orders lies with the ordering agency on a day-to-day basis, but that his organization

asks to be included in the discussion when disagreements arise. In response to a follow-up question, Mr. Verhulst stated that when small businesses have a disagreement, his organization tries to mediate and bring the issue to closure. He also explained that when the Small Business Governmentwide Acquisition Center awards a new small business contract, the Center actively engages in outreach throughout the country to familiarize the community with the vehicle and with GSA.

Panel Member Frank Anderson asked Mr. Verhulst what he believes are the most significant issues with the use of GWACs. Mr. Verhulst replied that the problems that he has read about stem from shortfalls at the ordering activity. He described interagency contracting as the current *"flash point of attention,"* and that GSA, in conjunction with OMB, is responding by instituting additional controls. He added that he would like to see more focus on training, and roles and responsibilities between the parties – contracting offices, requiring offices, ordering offices. Panel Chair Marcia Madsen thanked Mr. Verhulst for his insight, and suggested that he may be invited to a working group meeting to share additional insight.

Panel Chair Marcia Madsen introduced the next Panel presenters, Mr. Robert (Steve) Ayers, Senior Vice President, Contracts, Procurement and Ethics of Science Applications International Corporation (SAIC). Mr. Larry Trammel, SAIC's Senior Vice President for IT and Chairman of the Board of the Contract Services Association (CSA), accompanied Mr. Ayers. Panel Member Marshall Doke announced that because his firm represents SAIC, he would not be participating in the proceedings and moved from the stage area to the audience section of the venue. In his prepared statement (Attachment 5) and accompanying briefing entitled "*10 Steps Towards Improving Federal Acquisition of Services,*" Mr. Ayers introduced ten topics in Federal acquisition and a perspective on each (Attachment 6). Topics included performance-based service acquisitions (PBSA), cascading set-asides, subcontractor costs under T&M contracts, post-award audits, organizational conflicts of interest (OCI), low-cost versus best value approaches, fragmentation of acquisition policy, lack of transparency in rulemaking, early input/intervention in the rulemaking process, and institutionalizing an approach to lessons learned.

In response to questions from Panel Chair Marcia Madsen, Mr. Ayers elaborated on previous comments on PBSA. He indicated that a team approach to a PBSA requirements definition reduces the Program Manager's sense of lost control. He said that while he realized that PBSA is mandated, some requirements do not lend themselves to the approach, including the requirement for a subject matter expert where no true deliverable is required, and application of metrics and final acceptance criteria are difficult. Mr. Trammell said different Government agencies have expressed a need for PBSA templates, examples, metrics and best practices.

Panel Chair Marcia Madsen asked for clarification on previous statements regarding cascading set-asides. Mr. Ayers responded that even though better advanced planning would improve outcomes, in general, the approach should not be utilized. Mr. Trammel stated that large companies are less likely to bid for requirements that are competed using a cascading approach because company bid and proposal costs are required to be expended for a requirement where the likelihood of success has been reduced.

After agreeing that OCI policies across Federal agencies are inconsistent, Panel Member Ty Hughes asked Mr. Ayers to comment on OCI mitigation plan best practices. Noting that OCI issues are of great concern to SAIC because of its many different customers, platforms, and systems, Mr. Ayers suggested that geographic and organizational separation, execution of non-disclosure agreements, as well as full disclosure to prospective customers are the key activities for success. He offered to provide copies of successful OCI mitigation plans to the Panel. Asked by Mr. Hughes if there is a need to explore individual conduct and the financial interests of contractors working in program offices, Mr. Ayers and Mr. Trammel replied that they do not view this as the issue, adding that vigilance is critical and that the 250 member companies of CSA have ethics programs.

In response to a question regarding industry involvement in crafting agency operating procedures from Panel Member David Javdan, Mr. Ayers expressed concern over the emerging practice of removing internal agency procedural and policy guidance from the FAR supplement as it makes it hard for companies to track. Panel Member Frank Anderson commented that issues arise when agencies do not consult contractors when guidance impacting the relationship between contractors and buying organizations is changed, and that there is a *"gray line"* between what is guidance to *all* in the acquisition community, and what is truly internal. Panel Member Ty Hughes distinguished between contractor access to internal rules from those that are subject to rulemaking, and noted that with the experience of the workforce diminishing, access to guidance is particularly important.

Panel Chair Marcia Madsen stated that the Panel would be reviewing the distinction between what is *"inherently governmental,"* given that increasingly more functions are being performed by the private sector, and that the distinction between personal and non-personal services has, to a degree, been lost. She thanked Mr. Ayers and Mr. Trammel for their insight and suggested that they may be invited to a working group meeting to share additional insight.

Panel Chair Marcia Madsen introduced Mr. John Young, Vice President of Corporate Contracts and Pricing at Northrop Grumman. Stating that his firm represents Northrop Grumman, Panel Member Marshall Doke recused himself from the Panel for the duration of Mr. Young's presentation (Attachment 7). Mr. Young provided a very brief overview of Northrop Grumman, its capabilities and sales ($7B in Services out of $30B in Government Sales for 2004). Overall, he stated, service contracting has been a positive experience for Northrop Grumman. He said that here has been an increased opportunity to provide services traditionally performed by the military services. He cited an example of civilians currently operating forklifts that used to be operated by enlisted men, thus freeing up the soldiers to be protecting the peace in Baghdad.

Mr. Young discussed the increased awareness and recognition of the benefits of the Safety Act in providing liability protection for anti-terrorism-type services. He explained that a catastrophic terrorist attack would exceed the insurance limitations of large companies and ultimately result in destruction of the company. He noted that a current Transportation Security Administration solicitation allows offerors to provide proposals contingent upon Safety Act approval. Mr. Young then discussed the increasing use of multiple award pre-negotiated GSA agreements, GWACs and other agency agreements which have streamlined procurement processes and significantly reduce both cycle time and the cost of doing business for both Government and

industry. He provided examples from the U.S. Army Communications and Electronics Command's Rapid Response and the Navy's Sea-Port-E programs.

Mr. Young recommended that instead of legislation to limit the amount of profit or burden/overheads allowable on subcontract costs at the prime level, the marketplace be allowed to dictate what bidders receive as a reasonable profit on these allowable costs in accordance with Government-approved rates. He said to do otherwise is inconsistent with the way prime contractors price and manage their subcontracts. Additionally, he recommended that the definition of 'commercial service' be simplified, and the requirement that stand-alone services be based on established catalog or market prices for specific tasks or outcomes be eliminated. Mr. Young recommended a statutory change be made permitting T&M and labor hour contracts to be used in sole source situations when price reasonableness is supported. He stated that with consolidation in the defense industry, OCI issues have taken on increasing importance. He stressed that OCI mitigation requirements need to be consistently applied across and within agencies. Mr. Young concluded his presentation by returning to the subject of insurance coverage for terrorism events and the importance of the Safety Act, particularly with the increased exposure inherent in providing service in civilian environments. He explained that the lengthy wait required to secure a Safety Act approval creates a high risk situation for contractors because proposals are submitted prior to knowing if approval will be granted.

Panel Chair Marcia Madsen asked Mr. Young to expand on statutory changes associated with T&M and labor hour contracts when price reasonableness is supported. Mr. Young replied that the focus on determining price reasonableness is comparative analysis – historical or correlations to other products, but that this *"doesn't have to be certifiable, it just has to be demonstratable."* Panel Member Ty Hughes said he was intrigued by *"the concept of something not quite cost or pricing data, but something more than nothing."* He asked Mr. Young if industry is reluctant to share estimating models because of their proprietary nature. Mr. Young replied that while companies are doing very little true modeling, the models are considered very sensitive.

In response to a question from Panel Member Roger Waldron on the level of subcontract activity on service contracts, Mr. Young stated that for services in 2004, the total was approximately $3B and explained that the vehicles with subcontractors are usually T&M and labor hour. Mr. Waldron asked Mr. Young to comment on the impact of allowing Government cost reimbursement to prime contractors of subcontractor labor rates, not labor rates invoiced at a higher prime contractor rate, and if this would impact the level of subcontracting to small businesses. Mr. Young described a conflicting Sea-Port-E pre-award arrangement, later rescinded, wherein subcontractor rates could not be burdened at the same time prime contractors were incentived to increase the number of small businesses utilized. Mr. Young said he did not think a situation where a prime contractor prices subcontractor rates at the higher prime rates is appropriate, but that burdening subcontractor rates in accordance with negotiated forward pricing agreements should be allowable. Mr. Waldron asked Mr. Young if the growing number of multiple award contracts impacts whether Northrop Grumman bids for requirements. Mr. Young replied that his company is adjusting to the numbers and changing its business processes to accommodate the change.

In response to a request from Panel Chair Marcia Madsen, Mr. Young agreed to provide information on organizational conflict of interest documentation. Panel Member Ty Hughes asked Mr. Young to comment on what he believes is driving mergers and acquisitions, particularly of small engineering firms. Mr. Young said that large firms look for niche capabilities or intellectual property in order to leverage into a new market. He added that often acquiring the capability is less costly both in terms of money and time.

Panel Chair Marcia Madsen asked Mr. Young to consider attending a working group meeting to discuss OCI and inherently governmental functions in more detail. She thanked him for his presentation and insight into issues relevant to the Panel.

Panel Chair Marcia Madsen introduced Mr. Blaine Manson, Director of Contracts, Naval Air Warfare Center Weapons Division (NAWCWD), China Lake, and thanked him for speaking at the Panel meeting. Mr. Manson provided a brief overview of the mission and types of products and services that NAWCWD provides to the warfighter at China Lake, Point Mugu, and North Island. The Center contracts for approximately $450M, 79% of which is for services. Mr. Manson provided a field perspective on several issues that had been raised during previous presentations. He explained that notwithstanding training classes for the contracting and technical communities on performance-based contracting for services, he does not feel there is yet a viable example of a statement of work for intellectual support services. Mr. Manson believes that time and material contract vehicles for professional services are enabling the contractor to receive significantly more profit than on previously utilized cost-plus fee vehicles.

Stating that his organization has not yet executed Sea-Port-E orders, he explained that the Navy's policy is that Sea-Port-E contracts are the mandatory contracts of choice for NAVSEA, Naval Air Systems Command (NAVAIR), SPAWAR, Naval Supply Systems Command (NAVSUP) & Marines unless a waiver is received. His review of Sea-Port-E Procurement Administrative Lead Time ("PALT"), the time it takes to process an order, indicates that relative to traditional contracting, there is a 20 day savings which he attributes to elimination of the requirement to synopsize requirements on FEDBIZOPPS for Sea-Port-E orders. Mr. Manson explained that in the first round of establishing Sea-Port-E contracts, all but one offeror was awarded a contract. The next round resulted in award of 503 contracts from 512 proposals. Mr. Manson said that 492 contracts are available in the Southwest Region under which to place orders in 22 functional areas. Because procurement lead time and resources required to make award are very efficient for his existing Division I contracts for Engineering Services, he has received a waiver to allow their continued use. He said that Sea-Port-E contract orders are either cost or fixed price; there is no ability to award T&M orders. Sea-Port-E also allows for cascading awards where small business is provided the first opportunity for award.

In response to a question from Panel Member Roger Waldron, Mr. Manson briefly described the business case he believes the Navy used to establish Sea-Port-E. He said that NAVSEA felt that they could save from 6-8 % by establishing Sea-Port-E instead of utilizing GSA schedules, and that development of a web-based system would allow for an easier acquisition process. He added that use of Sea-Port-E will increase competition and establish common Navy-wide processes, but did not know why the ability to award T&M orders is not a Sea-Port-E feature.

He said that the Chief of Naval Operations is looking for a 4 – 5 percent savings overall for the fleet.

In response to a question regarding applicability of the Service Contract Act posed by Panel Member Frank Anderson, Mr. Manson explained that a Department of Labor wage determination is requested when required. For professional services, the requirement is reviewed to determine if labor categories covered by the Service Contract Act are included.

Panel Chair Marcia Madsen asked Mr. Manson about the extent to which Governmentwide contract vehicles are utilized by his organization to satisfy their requirements. He replied that 10 percent of the actions representing less than ½ percent of the dollars are awarded under GSA schedules. The organization no longer utilizes NAVSUP vehicles for IT hardware or Army basic ordering agreements for Oracle software. Ms. Madsen thanked Mr. Manson for his presentation to the Panel.

Panel Chair Marcia Madsen introduced Mr. Richard Hollis, Chairman and CEO of Hollis-Eden Pharmaceuticals, who had requested an opportunity to address the Panel to discuss procurement issues related to BioShield and Health and Human Services (HHS). In his remarks and prepared written public statement (Attachment 8), Mr. Hollis explained that his firm manufactures Neumune, the first medical countermeasure being developed to address acute radiation sickness. Mr. Hollis said that the difficulty and massive expense associated with development and approval of a new drug, as well as the fact the Government is the only customer, has deterred private investment in biodefense. Other factors include lower profit margins, political vulnerability and questions relating to liability and patent protection. Mr. Hollis expressed his strong support of the Federal Government's $5.6B multiyear BioShield program to foster the private sector biodefense industry. As envisioned by Congress, under the program, Department of Homeland Security (DHS) and HHS identify biological threats and HHS enters into early stage advance purchase contracts with companies that have the potential of developing counters to those threats. These companies then capitalize drug development through private markets resulting in a shift of risk to the companies and their investors.

Mr. Hollis expressed his concerns that the DHS & HHS approach to determining biological threats is bureaucratic, and the issuance of solicitations has been slow. He believes the Government's approach has not sent a positive message to capital markets. He noted that even with significant scientific progress and FDA approval to progress trials of Neumune to humans, his company's stock value has declined, contrary to what he believes would occur for similar accomplishments for drugs to treat cancer or heart disease. He believes that the consequences of reduced investments not only impact individual companies, but leave U.S citizens vulnerable. In closing his formal remarks, Mr. Hollis made five key recommendations: 1) DHS and HHS should quickly issue material threat assessments; 2) HHS should make a concerted effort to accelerate the procurement processes; 3) HHS should establish a process by which companies can be qualified for BioShield contracts; 4) requests for proposal (RFPs) should be continually open to correspond to threats; and 5) contracts should be sized to ensure adequate company return on investment.

Panel Chair Marcia Madsen thanked Mr. Hollis for his remarks, but noted that the Panel's charter was limited to procurement issues. Panel Member Jonathan Etherton asked Mr. Hollis if, in his opinion, the law establishing the authority for BioShield needs amending. Mr. Hollis answered that BioShield II legislation may be proposed that addresses patent and liability issues; however, he is a strong proponent of the original BioShield legislation and believes it would be effective if implemented appropriately.

Panel Member Ty Hughes asked Mr. Hollis how it is possible to negotiate terms and conditions on BioShield advance procurement contracts. Mr. Hollis explained that DHS material threat assessments assess vulnerabilities, countermeasures required, the level of drug stockpiling expected and the size and scope of the market. Mr. Hughes noted that in the Department of Defense (DoD), systems development contracts are usually cost contracts, and asked Mr. Hollis how a price agreement is reached under BioShield advanced purchase contracts when the parties do not know how much investment will be required to develop a drug. Mr. Hollis responded that with a DHS/HHS dosage requirement and the amount the Government is willing to spend, drug companies have enough information to determine if they wish to proceed. He said that the failure to provide dosage information during the four years since DoD requested development of Neumune has meant that Hollis-Eden is developing a medical countermeasure with no defined market. Mr. Hollis introduced his firm's Senior Vice President, Mr. Bob Marsella who provided additional information on the cost of drug development. Additionally, he noted that Government officials have responded to their concerns by telling the company to approach the National Institutes of Health (NIH) for assistance in developing their drug until the company becomes BioShield eligible.

In response to question from Panel Member David Javdan, Mr. Hollis said that NIH did not receive radiation grant funding until this year, and the company has received no Government funding to date from any source. He added that when DoD approached the company in 2001, no BioShield program existed, but the company believed that the U.S. Government would procure their countermeasure drug. He closed his remarks by stating that BioShield was intended to be a procurement bill and, therefore, he believes the company's concerns regarding implementation of BioShield make it an appropriate issue for the Acquisition Advisory Panel.

Panel Member Marcia Madsen thanked Mr. Hollis for his presentation and suggested that the issue may fall within the Panel's purview by virtue of Hollis-Eden's business size. She then thanked all the presenters and Panel members for their attendance at the Panel meeting.

Below is a list of additional materials or information requested by the Panel during the guest speakers' presentations:

- Ms. Ellen Polen – SPAWAR
    - Average size of task order on the ELITE contracts
    - Award term frameworks on MSA & ELITE contracts
    - Copy of briefing on NAVSEA Sea-Port E Contracts
    - Data on PBSA Standards for Award Term Evaluations
    - Representative sample task orders for various requirements including "people-time" and pure taskings.

- Mr. Michael Clancy – Oracle
    - Information on whether there are Oracle subcontracts for telephone support service or other software service support (to include consultants)
    - Information on specific cost savings the Government would accrue from pre-payment of software support
- Mr. Matt Verhulst - Small Business Governmentwide Acquisition Center, GSA
    - Metrics on Department of Defense's utilization of GWACs (Percentage of total GWAC Orders)
    - Training materials on fair opportunity (including exceptions and circumstances when they are used)
    - Contracting Officer delegation of authority
- Mr. Robert (Steve) Ayers, Senior Vice President, Contracts, SAIC
    - Information on Best Practices on team approach to performance-based contracting
    - Examples of successful OCI mitigation plans
- Mr. John Young, Vice President of Corporate Contracts & Pricing, Northrop Grumman
    - OCI Information for SMC

ADJOURNMENT

The ninth Acquisition Advisory Panel meeting was adjourned at approximately 04:25 P.M.

I hereby certify that, to the best of my knowledge, the foregoing minutes are accurate and complete.

10/25/05

Ms. Marcia G. Madsen
Chair
Acquisition Advisory Panel

Attachment 1

DRAFT

Statement of NCMA
To the
SERVICES ACQUISITION ADVISORY ("1423") PANEL

Madam Chair and distinguished members of the Services Acquisition Advisory Panel:

On behalf of the President and the 17,500 members that comprise the National Contract Management Association, we commend you on the vital work that your panel has done and continues to do and we thank you for the opportunity to address this body today. We are especially pleased that you have chosen this day and this location – at the site of our annual Aerospace and Defense Conference – to hold this public meeting of the Panel. And we are also proud to count several members of the Panel among our membership.

While NCMA is a non-lobbying organization and has maintained throughout the association's 45-year history its position as a neutral forum for exchange of ideas between buyers and sellers, NCMA also has worked over the years to promote improvements in the efficiency and effectiveness of the public procurement process, most notably in the acquisition reform movement of the 1990s and that interest continues here today.

NCMA would like to focus its remarks on the workforce issues facing the Federal government in the procurement function. We share many of the same concerns on the Federal procurement workforce as have been expressed by previous speakers before the Panel and by the Panel itself: decreasing size of the workforce at the same time that

workload as measured in dollars and complexity is increasing; gaps in competency especially in respect to performance-based acquisition, best value source selection, general business expertise and savvy, and adoption of appropriate commercial practices; attracting well-qualified, talented entry-level personnel to enter the profession of contract management and the Federal procurement workforce; increasing competition among Federal agencies for a limited pool of experienced journeyman contracting officers, specialists and administrators; and a looming problem with succession to the executive ranks in the Federal procurement workforce.

NCMA, within its resources, is working to address these issues. In the area of competencies, in recent years NCMA has completely revised its Contract Management Body of Knowledge or CMBOK to include commercial contracting and general business competencies. Concurrently we have expanded our educational offerings to cover topics such as risk management, financial aspects of contracts, negotiations skills, project management, recent changes to the Uniform Commercial Code, and this year we will publish a new book on performance-based acquisition as well as launching a new full-day seminar on that topic. NCMA has also teamed with the Defense Acquisition University, the Federal Acquisition Institute, and private sector training firms to encourage broadening of educational and training opportunities for the workforce. Further, NCMA restructured its certification programs, now consisting of a certification in Federal contracting, CFCM, certification in Commercial contracting, CCCM, and capstone certification, CPCM, to reflect the broader competencies demanded of a contract management professional today.

NCMA has made attracting well-qualified, talented entry-level personnel to enter the profession of contract management a key objective in its strategic plan for the future. In the last year we formed a University Outreach and Relations Committee and populated it with talented academicians as well as others with a strong interest in and connection to students and recent college graduates, we created a new membership category for students, we have made it more attractive for employers (including the Federal government) to post their entry-level job positions on NCMA's employment website, and we have planted the seeds for Student Chapters around the country. All of these efforts are designed to build awareness of contract management as a profession, encourage expansion of college and university programs in this field, and most importantly, to connect young people to mentors serving in this field and to future careers in procurement.

The challenges of increasing competition among Federal agencies for a limited pool of experienced journeyman contracting officers, specialists and administrators and a looming problem with succession to the executive ranks in the Federal procurement workforce are largely shared by the private sector, especially firms that do business with the Defense Department and the Federal government generally. This situation has its roots in the "Peace Dividend" of the early 1990s and a long series of years in which the Defense acquisition workforce was reduced in size, Defense prime contractors collapsed from many to only a few, and Defense spending was flat or reduced. During this nearly ten-year period hiring of new entry level personnel all but stopped and a "bathtub" in the

workforce was created. As the age of the workforce increases each year, this bathtub moves further to the right and is now being felt in a pronounced shortage of experienced journeyman-level contracting professionals. In another few years this bathtub will also impact at the executive level.

As a result, the Federal agencies are in relentless competition with one another for talented procurement professionals. But it is a fixed supply (due to barriers to entry into the Federal service, especially at other than the entry level) or a diminishing supply (due to retirements). NCMA encourages this panel to make recommendations that will help relieve some of these pressures. Specifically, NCMA encourages this panel to recommend adoption of appropriate professional credentials as a substitute for some or all of the mandatory training and education requirements for service in Federal procurement positions. Too often journeyman-level or senior contracting professionals from outside the Federal government are told that they can only qualify for entry-level Federal positions in the 1102 job series because they lack the mandated series of contracting courses at the 100, 200 and 300 level. Or, they face subtle discrimination in competing for mid-level and senior-level positions with current Federal employees because if selected they would have to spend their first weeks or months on the job going through mandatory training to "catch-up" with those who are already in the system.

We believe that this barrier for entry to Federal service in the 1102 series is harmful to attracting the best and brightest to civil service and is wasteful of limited human resources and training dollars. Individuals who have earned certification in the

contracting field as evidenced by holding the Certified Federal Contracts Manager or Certified Professional Contracts Manager designation have demonstrated mastery of many, if not all, the competencies acquired through the mandatory Federal training courses for 1102s. By adopting a formal policy of equivalence for professional certification in the contracting field the Federal government can remove one of the most daunting barriers to entry into the Federal procurement workforce for mid-level and senior professionals from industry. NCMA has been working towards this objective with the Defense Department for nearly two years now and would like to see this effort bear fruit and be expanded to the entire Federal government. While we can speak with credibility to only the contracting field, we believe in principle that the same barriers exist for other fields in the acquisition workforce, such as program management, logistics, and financial management, and that similar efforts to formally adopt equivalency policies apply equally in these fields.

In closing, NCMA would again like to commend the panel for the critical work it has done and continues to do in seeking to find ways to improve the Federal procurement process. NCMA appreciates having been given the opportunity to share its views today and welcomes the opportunity to contribute further to the Panel's work through or elected officers, members, and staff. Thank you.

The Space & Naval Warfare Systems Command

Acquisition Advisory Panel

Long Beach, CA

July 27, 2005

Ellen Polen
Corporate Contracts Branch Head
Space & Naval Warfare Systems Command

Space & Naval Warfare Systems Command

Who we are …

One of the Navy's five acquisition commands with 7,600 employees

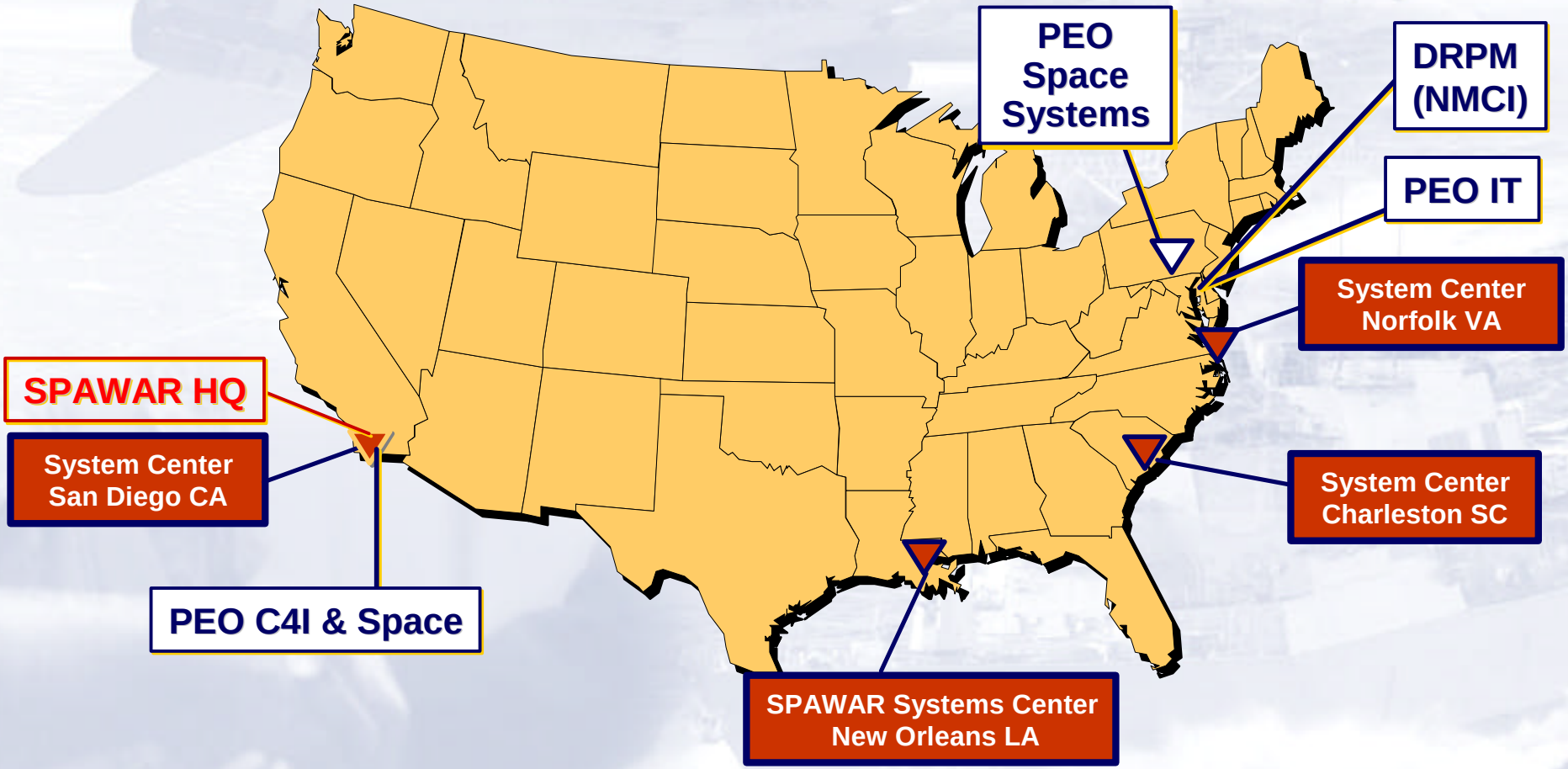
What we do…

- Partner with PEO- C4I & Space to deliver C4ISR and FORCEnet capability to the joint warfighter
- Partner with PEO-IT, DRPM (NMCI) & PEO Space Systems
- Develop Navy, Joint and Coalition Interoperability
- Navy C4ISR Chief Engineer
- Navy FORCEnet Chief Architect/Assessor
- Combined TOA $4.7 Billion

Mission, Vision & Commitment

- **Mission Statement:**
  SPAWAR Enterprise "delivers" FORCEnet – transforming information into decisive effects
- **Vision Statement:**
  "FORCEnet is the decisive weapon for the future Force"
- **Commitment:**
  - "We are dedicated to the Joint warfighters, who stand in harms way preserving our peace and defending our nation and its allies against aggression at home and abroad."

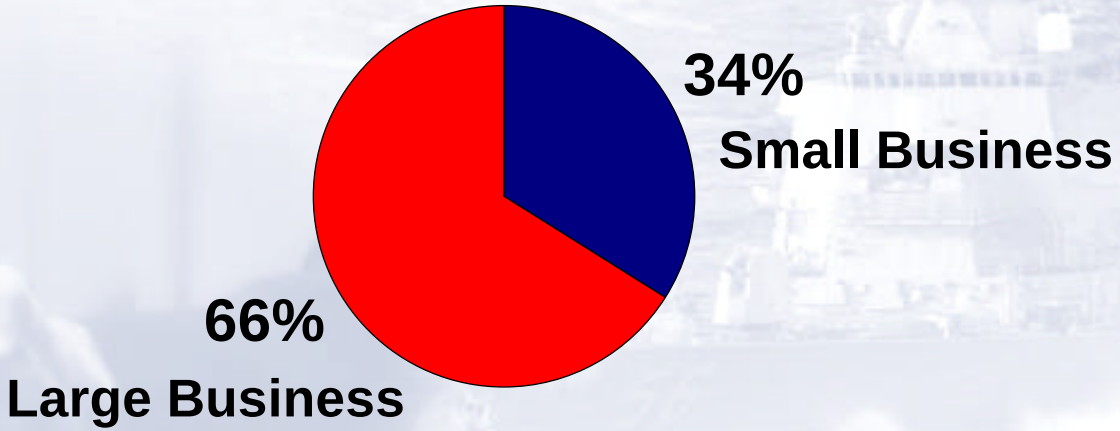
Corporate *SPAWAR*



"Transforming information into decisive effects."

SPAWAR Economics
(FY-04 data)

- **Total Contracts: $3.2B**
  - **San Diego alone: $1.8B**
  - **Other California $1.4B**



HQ Services Contracting Initiatives

- **FY – 04: Major Services Acquisition**
  - **PBSA Support Contract:**
    - Single Award 8(a) (GCC)
  - **Program Management:**
    - Multiple Awards (Anteon, BAH, MAXIM, and SAIC)
    - Unrestricted
    - IDIQ
    - Award Term
    - PBSA
  - **Engineering, Logistics, Installation, Test and Evaluation (ELITE) Contracts:**
    - Multiple Awards (Epsilon, INDUS, OSEC, Space & C4i, SYS, TCI and Tri-Star)
    - SBSA w/ at least one 8(a) Kr
    - IDIQ
    - Award Term
    - PBSA

(Total PBSA performance at HQ to date = 74%; OMB goal =40%)

Major Services Acquisition (MSA) Metrics

Description	PM Contracts	ELITE Contracts	Total
TOs Awarded	47	18	65
Total ceiling awarded (dollars)	$363.2M	$129.6M	$492.8M
Total ceiling awarded (hours)	4,176,961	1,424,408	5,601,369

Services Contracting Initiatives

- **FY- 05: Sea-Port Enhanced**
  - **Virtual SYSCOM Initiative**
  - **NAVSEA's Multiple-Award Engineering Services contracts**
  - **SPAWAR's implementation:**
    - **Zone 6**
    - **492 IDIQ contracts (364 are SB)**

SPAWAR's Sea-Port-e Implementation

- **Customer Outreach**
  - Briefed all Staff Codes and PMWs
  - Formed IPT to develop requirements
- **Industry Outreach**
  - 2 Industry Days
- **All Hands Training**
  - Web-Based e-Commerce Tool
  - Policies, Procedures and Templates
- **Current Status**
  - Approximately 20 HQ services acquisitions will be competed under Sea-Port-e in 4th Qtr FY-05
  - Estimated HQ Annual Value = $40M
  - SPAWAR Echelon II will also use Sea-Port-E

Policy Recommendations

- **Management Oversight Process for Acquisition of Services (MOPAS)**
  - **Align Acquisition Approvals**
    - **Current:**

Service	Total Planned Value	Approval Authority
Non-IT	<$500M	PEO – HCA - 02
Non-IT	Between $500M-$1B	DASN (ACQ)
IT	$32M in one year or $126M-$500M in all years	ASD (NII)
IT	>$500M	ASD (NII) via ASN (RDA)

    - **Recommend: Non-IT and IT Approval Authority remain at PEO – HCA - 02 under $500M**

Attachment 3

PRESENTATION FOR ACQUISITION ADVISORY PANEL SERVICES CONTRACTS JULY 27, 2005

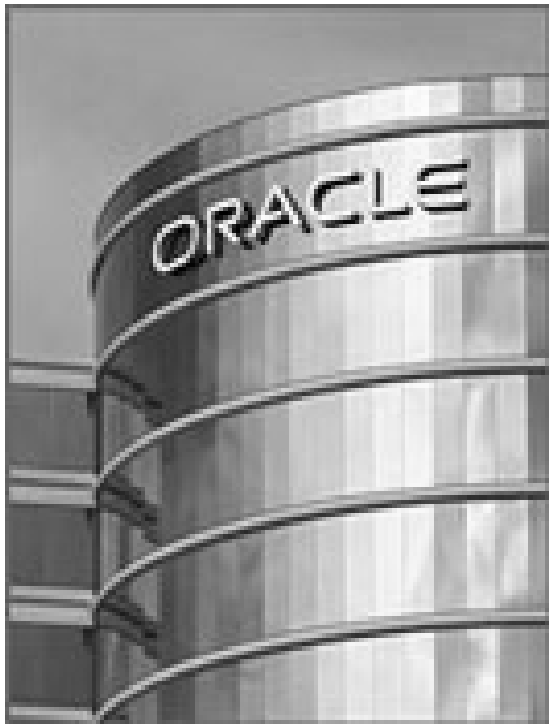
Michael Clancy
Chief Counsel
Government Sector & Compliance
Oracle Legal Department
703-364-2722
michael.clancy@oracle.com

ORACLE OVERVIEW

- **$11.799 billion (Total revenues/FY05)**

- **Software Business**
  - **Oracle Database, middleware & applications**
  - **Software license updates**

- **Services Business**
  - **Consulting: Design, implementation, deployment, upgrade and migration services for Oracle's software**
  - **Staff augmentation**
  - **Product support services**
  - **Education (Oracle University)**



ORACLE OVERVIEW

- **50,000 Employees Worldwide**
- **260,000+ Total Customers**
  - **Businesses of many sizes & industries**
  - **Federal, state & local governmental entities**
  - **Educational institutions**
  - **Resellers**

ORACLE INDUSTRIES

- Aerospace & Defense
- Automotive
- Communications
- Consumer Products
- Chemicals
- Education & Research
- Engineering & Construction
- Financial Services
- Healthcare
- High Technology
- Industrial Manufacturing
- Life Sciences
- Media & Entertainment
- Natural Resources
- Oil & Gas
- Professional Services
- Public Sector
- Retail
- Travel & Transportation
- Utilities

COMMERCIAL PRACTICES

- **Overview of Commercial Practices**
- **Comparison of Government and Standard Commercial Terms**
- **Recommendations**

COMMERCIAL PRACTICES

- **Consulting Services: Time & Material Contracts**
  - **Primary business model**
  - **Contract for services**
  - **Includes description of services**
  - **Labor categories for consultants with fixed hourly rates. For example:**
    - **Practice Director**
    - **Technical Director**
    - **Senior Principal**
    - **Associate**
  - **May specify use of offshore resources**

COMMERCIAL PRACTICES

- **Consulting Services: Time & Material Contracts**
  - **Estimated fee**
  - **No submission of cost data**
  - **Estimated completion date and, for complex engagements, there may be an estimated timeline for completion of stages of the project (e.g., design phase, build phase, test phase, and go-live date)**

COMMERCIAL PRACTICES

- **Consulting Services: Time & Material Contracts**
  - **Services provided on a T&M basis and payment is for actual time performing services plus materials and expenses**
  - **Payment is not based on acceptance of a deliverable or completion date**
  - **Shared risk provisions negotiated in some contracts; for example, larger, more complex engagements**

COMMERCIAL PRACTICES

- **Consulting Services: Time & Material Contracts**
  - **Data Rights**
    - **Oracle retains ownership and all intellectual property rights to anything developed or delivered under the agreement**
    - **Customer receives a non-exclusive, non-assignable royalty free license to use anything developed and delivered by Oracle for its internal business operations only**

COMPARISON OF GOVERNMENT AND STANDARD COMMERCIAL CONTRACT TERMS

WARRANTY

GOVERNMENT

- **FAR 52.212-4(o): "[I]tems delivered … are merchantable and fit for use for the particular purpose described in this contract"**
- **See also FAR 12.404(a)**
- **FAR 12.404(b)(2): states that it "may" be customary to exclude implied warranties**

COMMERCIAL

- **Services will be provided in a professional manner consistent with industry standards**
- **Warranty is exclusive**
- **No other express or implied warranties or conditions, including warranties or conditions of merchantability and fitness for a particular purpose**
- **Warranty period: 90 days after performance of the services**

REMEDY FOR BREACH OF WARRANTY & LIMITATION OF LIABILITY

GOVERNMENT

- **FAR 52.212-4(a): "Re-performance of nonconforming services at no increase in contract price"**
- **FAR 52.212-4(m),Termination for cause: "Contractor shall be liable to the Government for any and all rights and remedies provided by law."**
- **FAR 12.403(c)(2): "Government's preferred remedy … excess reprocurement costs" and "incidental or consequential damages incurred" due to termination**

COMMERCIAL

- **Exclusive Remedy**
- **Re-performance of deficient services**
- **If breach cannot be corrected in a commercially reasonable manner, customer may recover fees paid for the deficient services**
- **Maximum liability: total fees paid**
- **No excess reprocurement costs**
- **No indirect, incidental, special, punitive or consequential damages**

AUDIT RIGHTS

GOVERNMENT

- FAR 52.212-5 (d) and 52.215-2
- 3 years after final payment

COMMERCIAL

- In limited circumstances (for example, engagement with a significant fee estimate)
- Contract may provide for supporting documentation (e.g., time sheets) for a specific invoice pursuant to a written request
- Short time limit -- for example, 4 months from the date of the applicable invoice

PREPAYMENT

GOVERNMENT

- **No advance payment**
- **Payment may not be more than the value of the service already provided (31 U.S.C. 3324)**
- **Payment for services rendered and accepted (FAR 52.232-1)**

COMMERCIAL

- **For software support services, payment yearly in advance**
- **Commercial business practice & financial systems modified for Government to provide for payment in arrears**

MOST FAVORED CUSTOMER CLAUSES

GOVERNMENT

- **GSA Schedule – Price Reduction Clause and tracking customer**

COMMERCIAL

- **No most favored customer clause**

RECOMMENDATIONS

- **Time & Materials Contracts**
  - **Expand definition of Commercial Items to clearly include T&M contracts for consulting services**
  - **Eliminate restriction that T&M can only be used if there is a determination and finding that no other contract type is suitable**
  - **Expand FAR Part 12 to include specific subparts to address commercial services and T&M consulting services**
- **Express statutory authority for prepayment of software support services**
- **Reduce time period for audit of T&M invoices to a commercially reasonable time of 6 months**

RECOMMENDATIONS

- **Expressly adopt commercial remedies, the exclusion of implied warranties, and limitations on damages (i.e., no excess reprocurement costs and no consequential damages)**

- **Adopt commercial data rights terms for consulting services (see FAR 12.212 which provides that Government's rights in commercial software shall be defined by commercial license terms)**

- **Promote competition and eliminate Price Reductions clause**

QUESTIONS
ANSWERS


ORACLE®

Attachment 4

GSA Federal Supply Service

GWACs

GOVERNMENTWIDE ACQUISITION CONTRACTS

SARA

Acquisition Advisory Panel

Long Beach, CA

July 27, 2005

Matt T. Verhulst

Acquisition Excellence

Presentation Outline

- “GWAC” Defined
- Authority & Reporting
- “Get It Right” Plan
- Benefits
- Access
- Ordering
- GSA’s GWACs

What is a GWAC?

A *Governmentwide Acquisition Contract* is defined as a task or delivery order contract for information technology (IT).

- Contracts established by one agency for Governmentwide use
- Operated by an Executive Agency designated by the OMB
- Pursuant to Section 5112(e) of the Clinger-Cohen Act, 40 U.S.C 1412

Authority to Award GWACs

- Derived from the Clinger-Cohen Act
- OMB oversees GWACs
- OMB designates an Executive Agent to award and manage each GWAC
- Executive Agents report to OMB

OMB Reporting and Contract Oversight

- Scope (required to review each order > $100K)
- Competition (no. of quotes or offers received per order)
- Order value
- Estimated task order value for Period of Performance
- Socio-economic volume
- Fair Opportunity Exceptions
- Task order type
- Number of Task Orders with Performance Based Terms
- Increased reporting on interagency contracting in new Executive Agent designation

Get It Right

GSA Initiative in concert with DOD

1. Secure the best value for federal agencies and American taxpayers through an efficient and effective acquisition process, while ensuring full and open competition, and instilling integrity and transparency in the use of GSA contracting vehicles.
2. Make acquisition policies, regulations, and procedures clear and explicit.
3. Improve education and training of the federal acquisition workforce.

L13

Get It Right

GSA Initiative in coordination with DOD

4. Ensure compliance with federal acquisition policies, regulations, and procedures.
5. Communicate with the acquisition community, including agencies, industry partners, OMB Congress and other stakeholders regarding the use of contracting vehicles.

www.gsa.gov/getitright

Benefits

- FAR compliant
- Full and open competition met/ ease of use
- Broad IT work scope
- Pre-qualified contractors
- Dual levels of competition
- Range of contract types & order terms
- Direct ordering available
- Limited protestability
- Fair opportunity competition ensures Section 803 compliance
- E-Buy available for fair opportunity competition
- Effective contract management controls
- Tools available to assist with GWAC selection

Accessing the GWACs

- Contracting Activity – GWAC centers
- Requiring Activity – Normally internal. Establishes the requirements and performs project planning (such as IT capital planning requirements).
- Ordering Activity – Internal or external. When internal, the service is usually an overhead function. When external, the service is usually fee based and is often named “assisted services”. Direct contract access is available given proper credentials, training and agreements. The ordering activity manages:
    - acquisition
    - administration
    - close out

Ordering Steps

Outline View

1. Sign MOU with GSA (if not GSA), present warrant, receive training, and obtain Delegation of Ordering Authority
2. Finalize the:
   - requirements
   - acquisition plan
   - file documentation
   - request for proposals (RFP) or request for quotations (RFQ)
3. Issue RFP or RFQ
4. Receive proposals/quotes
5. Evaluate proposals/quotes and select contractor
6. Issue task order
7. Administer task order
8. Close out task order

Contract Vehicles

ANSWER Millennia Alliant ITOP II	Enterprise GWAC Center
HUBZone 8(a) STARS Alliant SB VETS	Small Business GWAC Center
Millennia Lite Smart Card	Greater Southwest Acquisition Center

Enterprise GWAC Center

San Diego, CA

(877) 534-2208

www.gsa.gov/egc

ANSWER GWAC

- Awarded 1998
- MA/IDIQ
- Worldwide coverage
- 10 Industry Partners
- 10-year contract period of performance through December 31, 2008
- FFP, FPIF, FPAF, T&M and labor hour
- $25B ceiling
- Scope – a full complement of IT services

ANSWER GWAC

- **2,729** Projects awarded
- **$3.91** Billion Obligated
- **$7.96** Billion Estimated Value
- **147** Skill Levels
- **29** IT Functional Applications
- **7,454** Contractor Personnel
- **48/63** Coverage (States/Countries)

Millennia GWAC

- Awarded 1999
- Worldwide coverage
- $25B contract ceiling
- 9 Industry Partners
- Specifically designed for large scale IT projects
- 10-year contract period of performance
- Fixed Price and Cost Reimbursable tasks

Millennia GWAC

- **103** Projects Awarded
- **$4.29** Billion Obligated
- **$8.51** Billion Estimated Value
- **17** Skill Levels

Follow-On Procurements

- **ALLIANT** Contract will replace ANSWER and Millennia
  - URL: www.gsa.gov/alliant
- New Task Orders on ANSWER and Millennia may be issued **up to three months after the award of ALLIANT** and must be completed within five years

ITOP II GWAC

- DOT Contract transferred to GSA
- Awarded February 28, 1999
- Contract Ceiling $10 Billion
- New Task Orders can be issued up to January 27, 2006 for a period of five years
- All types of task orders available (FP, CR, T&M/LH)
- 187 task orders awarded
- $2.77 Billion obligated
- $5.25 Billion estimated value

Top 10 Customer Agencies – Enterprise GWAC Center*

Agency	Total Awarded
Dept of the Navy	$2.04 B
Dept of the Army	$1.73 B
Dept of the Air Force	$957.3 M
Dept of Defense	$835.3 M
Environmental Protection Agency	$504.8 M
NASA	$242.7 M
Dept of Health & Human Services	$196.5 M
GSA	$176.7 M
Dept of State	$134.0 M
Dept of Transportation	$114.4 M

**as of May 2005*

Small Business GWAC Center

Kansas City, Missouri

(877) 327-8732

www.gsa.gov/sbgwac

HUBZone GWAC

- **HUBZone: Historically Underutilized Business Zone**
  - HUBZone Act of 1997, Title VI of P.L. 105-135 created the HUBZone Empowerment Contracting Program
- **Goal:** Stimulate the economy and create jobs in areas of pervasive unemployment and underdevelopment

HUBZone GWAC

- Competitive Multiple-Award HUBZone set-aside
- Five-year contract (Jan ’03 – Jan ’08)
- Two-year base period, three one-year options
- Fixed price, labor-hour, and time & material terms
- $2.5 billion program ceiling
- Teaming arrangements with niche subcontractors
- Worldwide coverage, not limited to HUBZone area

HUBZone GWAC

- 34 HUBZone-certified Industry Partners
- Seven functional areas based on North American Industrial Classification System (NAICS) codes
- Eight to 10 contract awards in each functional area
- Nine of 34 firms with task orders worth $23.9 M
- Top 3 customers: DOJ, Navy, EPA

www.gsa.gov/hubzone

New! 8(a) STARS

- 8(a) Streamlined Technology Acquisition Resources for Services
- Competitive, multiple-award 8(a) set-aside
- Awarded pursuant to Section 8(a) of the Small Business Act (Public Law 85-536) and in accordance with the FAR Part 19

8(a) STARS GWAC

- Awarded May 2004
- Seven-year contract (2004 - 2011)
- Three-year base with two, two-year options
- Fixed price, labor-hour, and time & material terms
- Directed orders allowed up to $3 million. Fair opportunity process must be used for orders in excess of $3 million
- $15 billion program ceiling
- Worldwide coverage

8(a) STARS GWAC

- 432 8(a) certified Industry Partners
- Eight functional areas based on North American Industrial Classification System (NAICS) codes
- 100 of 432 firms with task orders worth $114 M
- Top 3 customer agencies: Air Force, Navy, DoD

www.gsa.gov/8astars

New! VETS GWAC

Veterans Technology Services (VETS)

- Executive Order 13360
- Competitive, multiple-award Service-Disabled Veteran-Owned Small Business set-aside
- Offers received July 15, 2005
- Currently evaluating offers
- Awards expected June 2006

www.gsa.gov/vetsgwac

New! Alliant SB GWACs

Alliant Small Business (Alliant SB)

- Competitive, multiple-award Small Business set-aside
- Scheduled for release August – September, 2005
- Awards expected Summer 2006

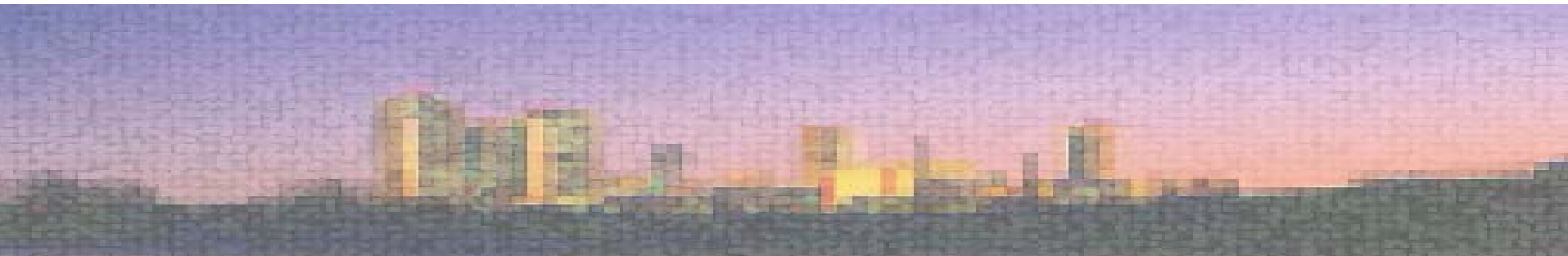
www.gsa.gov/alliantsb

Greater Southwest Acquisition Center

Fort Worth, TX

(877) 929-4822

www.gsa.gov/itgwaccenter



Millennia Lite GWAC

- Worldwide coverage
- Nationwide ceiling priced labor rates with provision for worldwide pricing
- 33 Industry Partners
- 37 contracts
- Contract period of performance: April 2000 – July 2010 *

* Based on Functional Area

Millennia Lite GWAC

- 3-year contract period
  - With performance-based extensions for a total 10-year contract period through 2010
- All types of task orders available (FP, CR, T&M/LH)
- $20 billion contract maximum
- As of March 31, 2005:
  - 1,388 task orders awarded
  - $2B awarded value
  - $7.1B estimated value (incl. options)

Smart Card GWAC

- 4 Industry Partners
- Contract Ordering Period expires May 17, 2006
- $1.5 billion program ceiling
  - Sales as of March 31, 2005: $212,922,843
- Firm, Fixed Price and Time and Material tasks
- Expert technical assistance available from GSA's Center for Smart Card Solutions

www.gsa.gov/smartcard

Questions?

Matt T. Verhulst

Contracts Director, GSA Small Business GWAC Center

Thank you

Attachment 5

Section 1423 Panel Meeting

Long Beach, Calif.

July 27, 2005

Steve Ayers

Senior Vice President,

Contracts and Procurement

Science Applications International Corp.

San Diego, Calif.

SAIC
From Science to Solutions™

10 Steps Toward Improving Federal Acquisition of Services

SAIC
From Science to Solutions™

Performance-Based Services Acquisition

- End-users uncomfortable with specifying the ‘what’ and leaving it to contractors to figure out the ‘how’
- RFPs simply recast SOWs as SOOs
- In order for PBSA to succeed, Government needs to overcome internal resistance through sustained awareness, training effort

Cascading Set-Asides

- Source selection process in which all categories of offerors—both large and small businesses—compete and agency then looks for winner by category
- Allows agency to avoid deciding its acquisition strategy at outset
- Forces offerors to waste B&P costs
- No FAR coverage

Subcontractor Costs Under Time and Materials Contracts

- DCAA disallowing profit on subcontracted effort
- Primes expend considerable effort in managing subcontracts
- Inherent risk in subcontracting
- Primes have a right to make a profit
- T&M contracts are a customary commercial practice
- Inconsistent treatment of ODCs

Post-Award Audits

- FARA did away with post-award audits of commercial item contracts
- GSA ANPR seeks to reinstate post-award audits
- No justification
  - Existing access to records sufficient
  - Burdensome, especially for SB
- Increase in pre-award audits should allay concerns

Organizational Conflicts of Interest

- Uneven application of policy allows clearly inappropriate activities yet is over-reaching
- Need to steer middle course that recognizes OCI mitigation plans

Low Cost vs. Best Value

- Tendency to award IT services to low-cost bidder encourages buying in
- Nearly 60% of all contracts result in increased costs
- Need to ensure price realism of proposed solution

Fragmentation of Acquisition Policy, Procedures, & Contracts

- Uniformity and consistency promised in FAR being undercut by agency-unique rules, systems, e.g., DHS, FAA
- GSA reorganization will require major adjustment
- Contractors burdened in having to keep up with multiple policies and duplicative IDIQ and MAC contracts

Lack of Transparency in Rulemaking

- Agencies removing guidance from regulations and placing in other locations
- Contractors forced to hunt down new repositories
- Need to ensure that all relevant guidance is readily accessible

Early Input/Intervention in Rulemaking Process

- Rulemaking process does not allow public input until tail end
- Providing for early awareness, involvement would avoid needless rework, delay
- Options:
  - Hold public meetings on agenda
  - Create mechanism within OFPP

Institutionalized Approach to Lessons Learned

- Establish Lessons Learned office in DAU
- Analyze procurements to determine what worked and what didn't

Conclusion

- Need to recognize that procurement of services takes place in commercial context
- Contractors need consistency
- Minimize nonvalue-added requirements
- Accept, work within limitations of system

Acquisition Advisory Panel

Hyatt Regency Long Beach, Long Beach, Calif.

July 27, 2005

Presentation of Steve Ayers,

SAIC Senior Vice President, Contracts and Procurement

Good afternoon, Madam Chair, Panel Members.

I am Steve Ayers of Science Applications International Corporation. I am responsible for contracting and procurement in SAIC. Accompanying me is Larry Trammell who is involved in business development. By way of context, SAIC, a Fortune 500® company, currently ranks as the eighth largest defense contractor and is the largest employee-owned research and engineering firm in the United States. SAIC and its subsidiaries have more than 43,000 employees with offices in over 150 cities worldwide and annual revenues of over $7 billion. We are predominately a provider of engineering and technical services to the federal government but also have a commercial business unit with over $500 million in revenues from information-centric work in the commercial energy and life sciences markets.

We very much appreciate the opportunity to address the Acquisition Advisory Panel. I am going to briefly cover 10 topics of concern to us. Some of these topics, among them cascading set-asides, are issue-specific, while others, such as organizational conflicts of interest and fragmentation of acquisition policymaking and practices, are overarching or process-oriented issues. We also offer a number of recommendations, or course corrections, if you will, that are intended to help you arrive at answers that will promote the effective and appropriate use of commercial practices and performance-based contracting. In addition to my remarks I am submitting for the record answers to several of the questions linked to your Web page concerning SAIC's commercial business.

1. Performance-based services acquisition. Let me begin with some observations on the state of practice in Performance-Based Services Acquisition. Although a generalization, most end-users that we support do not understand nor want to use performance-based contracting. They are comfortable with being able to specify what and how they want work performed and have not accepted the premise that they should focus on outcomes and let us find more efficient ways to get the job done. Many actually are concerned about "losing control" of the solution delivery if they just specify the outcomes. It will take a lot more education to change the culture of the end-users so that they embrace and reach for performance-based contracted support rather than view it as a top-down imposition of policy from the administration.

The current processes used for solicitations performance-based service contracts are very uneven. We see quite a few RFPs that claim to be performance based but are in reality "how to" statements of work—in fact, some are exact replicas of the previous procurement documentation, simply relabeled as a Statement of Objectives (SOO). Frequently, performance-based solicitations have measures and standards, but there is no linkage from performance to incentives and/or penalties. Many of these still engage an

award or incentive fee, but it's based entirely on a subjective evaluation of the contractor's performance. We also see solicitations using SOOs accompanied by significant resistance to providing the necessary baseline data that would enable a contractor to understand details of the outcomes necessary to be able to propose an improved and more cost effective and efficient way to get the desired outcomes.

If PBSA is going to achieve its promise, federal departments and agencies are going to have to mount a very significant and sustained effort to socialize and train end-users on the benefits of performance-based contracting that is focused on improved outcomes. The seven steps training provides some procedural help, but doesn't go the distance to changing the mindset of the community engaged in writing performance-based procurements.

2. Cascading set-asides. Another problematic area is the issue of cascading set-asides, also known as cascading procurements. What started as an experiment by the Department of Housing and Urban Development in awarding management and marketing contracts has now spread to a growing number of agencies, including the departments of Agriculture, Health and Human Services, and Veterans Affairs and the Air Force.

Cascading set-asides are a source selection process in which an agency invites all interested offerors—be they large businesses, HUBZones, 8(a) businesses, and so on to submit proposals at the same time. The evaluation process is then tiered—hence the term "cascading"—by socioeconomic category, beginning with the highest tier, HUBZone businesses, and then proceeding to 8(a) businesses, and so forth until the agency identifies a winner, at which point the competition comes to a halt. In the event no winner is selected from among the small business categories the source selection proceeds to the last category—unrestricted/full and open.

While this novel approach affords an agency a convenient way to avoid deciding its acquisition strategy at the outset, it forces competitors—both large and small—to expend bid and proposal costs needlessly. A portion of those costs, incidentally, are ultimately borne by the federal government.

Interestingly, nowhere does the term "cascading set-aside" appear in the Federal Acquisition Regulation (FAR). It is wholly the creation of agencies.

In sum, cascading set-asides is a bad idea.

3. Time and materials payment provisions. Another troubling development that has surfaced in recent months is the treatment of subcontracted costs under GSA schedules contracts that contain the time and materials payment clause. Defense Contract Audit Agency auditors are selectively disallowing profit on the subcontracted effort, thus limiting the prime contractor to charging the government only what the subcontractor in turn is charging the prime. DCAA has created a fiction in which subcontracted effort as treated as "material" rather than "time." This view is short-sighted, as it ignores not only the significant time and effort that primes must expend to manage their subcontracts but also the inherent risk entailed in such efforts. Subcontract costs can account for upwards of 50% of the total value of a contract. To expect a contractor to absorb such costs and risk is not only unfair but also counterproductive, as it will encourage contractors to take work in-house rather than place it with subcontractors. This would in turn be unfortunate for subcontractors, many of whom are small businesses. Government contractors, like

any other for-profit enterprise, have a legitimate right to be able to make a reasonable return on the entire contract. It would be unthinkable for a homeowner, having contracted with a general contractor to put an addition on his or her house, to expect that contractor to charge only what the individual carpenters, electricians, plumbers, etc. were paid on an hourly basis. So, too, it is grossly unfair to expect contractors providing services to the federal government to forgo profit on a substantial amount of their work.

Part of the problem, as Director of Defense Procurement and Acquisition Policy Deidre Lee acknowledged in a May 3 e-mail to the Information Technology Association of America, is that the existing T&M Payments clause at FAR 52.232-7 is oriented toward a non-commercial market, whereas the context in which it is being applied is commercial item procurement under the GSA schedules. Ms. Lee assured industry that the situation will be remedied. Two FAR cases have been opened. One would revise the existing clause for non-commercial items; the other would add a new payment clause that is geared specifically to the payment provisions needed for commercial items.

Meanwhile, as I speak, the Senate is considering putting language into the fiscal year 2006 defense authorization bill (S. 1042) that would allow prime contractors that use subcontracted labor to make a profit only at the level specified in the subcontract. Adoption of such language, particularly without benefit of any public hearing on the subject, would be most unfortunate.

It needs to be recognized that T&M contracts are a customary commercial practice that is successfully used in many situations where the customer is not buying an end item with acceptance criteria. T&M is a flexible approach that is appropriate whenever the extent or duration of the work cannot be estimated with certainty at the outset. It also should be recognized that contractors providing commercial services have a strong built-in incentive to manage their labor force—including subcontracted labor—efficiently.

A separate but related development is the inconsistent treatment of other direct costs—ancillary or incidental items obtained by agencies through the schedules vehicles. Some schedules contain explicit guidance on the use of ODCs while others provide none. GSA is drafting guidance on the treatment of ODCs to address this issue, but meanwhile, contractors are left in the lurch.

4. Post-award audits of GSA schedules contracts. Still another looming problem is the advance notice of proposed rulemaking (ANPR) issued by GSA March 11 and revised April 12 calls for revising the Examination of Records clause, GSAR 552.215-71, to reinstate post-award audit access to a GSA schedule contractor's records to verify that preaward/modification pricing, sales, or other data were accurate, current, and complete.

Comments were due May 10, and industry is waiting with bated breath for the next development.

Quite simply, the case for reinstating post-award audits has not been made. The Federal Acquisition Reform Act of 1996 (FARA), incorporated as Division D of the fiscal year 1996 National Defense Authorization Act (P.L. No. 104-106), eliminated post-award audits of commercial item contracts. Yet, only a few months later, GSA took it upon itself to propose regulations to permit post-award audits of certain commercial item contracts.

The House National Security (now Armed Services) Committee, in response, reiterated its intent in the report accompanying the FY 1997 National Defense Authorization Act (P.L. No. 104-563) reiterated its previously stated intent that "the only remaining authority for the government to pursue such information is the authority of the General Accounting Office to audit contractor records."

In yet another unequivocal expression of congressional intent that there be no post-award audits of commercial item contracts, the three primary authors of FARA—Sen. William Cohen (R-Maine), and Reps. William Clinger (R-Pa.) and Floyd Spence (R-S.C.)—wrote to the then-head of the Office of Management and Budget on Sept. 18, 1996 stating: "The clear intent of Congress was that these audits would no longer be performed by Federal agencies. Congress clearly did not intend that this statutory change permit Federal agencies to subsequently determine through agency supplements to the Federal Acquisition Regulation whether and to what extent post award audit access is appropriate on commercial item contracts."

The government's case for reinstating post-award audits rests in large part on a report by the Government Accountability Office criticizing GSA's administration of schedule contracts, "Contract Management: Opportunities to Improve Pricing of GSA Multiple Award Schedules Contracts" (GAO-05-229). GAO examined 62 MAS contracts—out of roughly 15,000—and determined that 37, which equates to nearly 60 percent, "lacked sufficient documentation to clearly establish that the contracts were effectively negotiated. Roughly 40 percent "lacked adequate price analysis or price negotiation documentation." But nowhere does GAO assert that the government was prejudiced as a result of these alleged lapses on GSA's part. Rather, it appears to be saying that there is the potential for a problem, based on a sample of less than half a percent.

The GSA inspector general also has expressed concerns with regard to MAS pricing. To the extent those concerns are valid, we emphasize that the time to conduct audits is upfront, at the preaward stage. The IG itself recognizes that, and has undertaken to substantially increase the number of preaward audits of GSA MAS contracts.

We contend that the fears of GAO and the GSA IG are largely unfounded. Given market forces, not to mention the recent statutory requirements for competition in placing orders under schedule contracts, contractors have a strong built-in incentive to offer competitive pricing.

The fact is that the government has ample access to a contractor's data. FAR 52.212-5 authorizes the Comptroller General to examine a contractor's directly pertinent records involving contractually related transactions. Also, GSAR 515.209-70(b) permits a contracting officer to modify the Examination of Records clause for other than MAS contracts to define a specific area of audit. For MAS contracts, GSAR 515.209-70(c) permits the contracting officer to modify the clause at 51.215-71 to provide for post-award access to and the right to examine records to verify that pre-award/modification pricing, sales or other data related to the supplies or services offered under the contract which formed the basis for award/modification was accurate, current, and complete." Before modifying the clause, the CO must determine that absent such access there is a likelihood of significant harm to the Government and obtain the approval of the Senior Procurement Executive.

Moreover, reinstating post-award audits would be highly burdensome, particularly for small businesses, which constitute approximately 80 percent of all schedule contractors. The records retention policies in FAR 4.7 do not contemplate retaining voluminous data for periods of more than 20 years (assuming the initial five-year base period of a MAS contract and exercise of three five-year options, plus three years after final payment).

Yet, in the face of all these strong arguments against reinstating post-award audits of commercial item procurements, GSA has taken it upon itself to initiate a rulemaking effort that would do just that.

5. Organizational conflicts of interest. Another specific policy and procedural area that we believe needs attention is organizational conflicts of interest. We would have no quarrel with the language on OCIs in FAR Part 9.5 if it were applied with reason. However, we are troubled by the uneven application of this policy. At one extreme we see where a technical services firm is allowed to continue to support government oversight of programs being developed by the very aerospace firm that purchased the technical services firm. At the other end of the spectrum, elements of a major buying command of a military department will not even consider an OCI mitigation plan—it is just black and white that OCI cannot be mitigated. The latter is very troubling because no one can define the limits on the reach of the OCI associated with a task under large, multiyear contracts like Seaport-e and multiyear platform programs that indirectly touch all kinds of subcomponents and related programs. We urge you to consider the over-reach of OCI and steer toward a policy that presumes, except in extraordinary circumstances, that appropriate mitigation plans and non-disclosure agreements will provide the government suitable protection against organizational conflicts of interest.

6. Low cost vs. best value awards. Another area that calls for attention is low cost vs. best value awards. This is directly applicable to evaluating performance-based contracts. At some time or other nearly all contractors lose a competition where the winning price is significantly lower—up to 25% lower—than the range of all the other bids. This means either the winning contractor did not understand the work or bid to win and not to perform. This is also known as "buying in."

We wondered about the post-award results of such low bids that the government accepted and hired Paul DeLottinville Communications to do an independent analysis of these bids. His conclusion: "Government buyers beware." The old adage has been affirmed: "You get what you pay for." Two-thirds or better of all federal government bids for IT outsourcing services are awarded to the low-cost bidder even though it is often a best-value competition. Unfortunately, nearly 60% of all contracts awarded to the low-cost bidder resulted in increased contract costs. This is because the awardee could not deliver the contracted services as promised and the government, to avoid another recompetiton, chose to renegotiate the contract for higher rates, more staffing, longer deliverable schedules, and augmented funding to fix problems. We recommend that you ensure that the procedures used in evaluating performance-based contracts take into account the price realism of the proposed solution, including the availability in the specific labor market of qualified personnel at the price offered.

7. Fragmentation of acquisition policy, procedures, and contracts. A further area that warrants attention is the continuing trend toward fragmentation of acquisition policy and procedures and indefinite delivery, indefinite quantity contracts and multi-agency contracts. It is very expensive to keep up with all the variations in acquisition policy that have developed because of the various streamlining efforts that have been legislated in recent years. We no longer have a single, uniform FAR to look to for guidance. The Department of Homeland Security has its still-evolving processes, the Federal Aviation Administration has its own acquisition system, the Department of Defense and the military departments continue to have unique processes added both by Congress and internally. In addition, each region of the General Services Administration seems to have a unique interpretation of acquisition policy.

SAIC is a long-time player in the federal market, so we work hard at keeping current on all these variations in policy and procedures. However, this jumble of policy, regulation, and procedure is a significant barrier to entry of commercial firms into the federal market. The government should strive for consistency and simplicity of process and procedure across departments, agencies, and regions if it wants to attract and retain talented players in the federal market.

As to the various IDIQ contracts, the question is: How much is enough? We believe the GSA schedules and GWACs have worked well but clearly did not have sufficient internal oversight to ensure sound acquisition policies were followed. It now seems as if every franchise fund and every agency wants to roll out it own IDIQ contract for services that is more or less a copy of the GSA Federal Supply Schedules or the GSA multi-award contracts. It costs companies a lot to bid on these duplicative contractual vehicles and it will cost the taxpayers a lot to administer them. If the legislation pending in the Senate becomes law we expect each of the military departments and the Defense Logistics Agency also will issue duplicative IDIQ contracts for services. It might be better to focus on getting the new GSA Federal Acquisition Service in place, ensure consistent policies are used across the regions, and then use that organization as the principal method—across all of government—for buying commercial goods and services. If the fragmentation continues, then I expect we will see more acquisition problems as the many organizations with multi-agency IDIQs compete for the federal customer and apply their local understanding of acquisition policy.

8. Lack of transparency in the rulemaking process. The increasing decentralization of acquisition policy and procedures is further complicated by the lack of transparency of the process. The American Bar Association Section of Public Contract Law, in a white paper discussed in August 2004 at the group's annual meeting, expressed concern over the tendency of federal agencies to carve out guidance from the Code of Federal Regulations and treat it as internal procedures. One example is the effort on the part of the National Aeronautics and Space Administration to subdivide the NASA FAR Supplement (NFS) into two parts—one for policies, procedures, and contract provisions, the other for internal administrative procedures that ostensibly have no bearing on the contracting relationship between NASA and its contractors. The Department of Veterans Affairs likewise has made a practice of not putting procurement-related procedures in its FAR supplement but rather having a separate repository that only those who are familiar with the agency's practices are able to access. Even the Defense Department is headed in

this direction; the ongoing effort to transform the DOD FAR Supplement (DFARS) is in large part being accomplished by removing chunks of material from the DFARS and placing them in a separate repository called Procedures, Guidance, and Information (PGI). Such practices complicate the private sector's dealings with agencies, forcing contractors needlessly to invest time and effort to track all relevant rules and guidance. A portion of the resulting costs ultimately is borne by the government customer. More important, such practices run counter to the principle of open government upon which this nation was founded. Moreover, they run counter to the e-Government initiative that is one of the pillars of the President's Management Agenda. We recommend that agencies be required to clearly post all of their procurement rules, procedures, guidance, and information on their Web sites. Further, we recommend that OFPP issue guidance delineating when it is and is not appropriate to carve out guidance from the FAR and FAR supplements.

9. Early input/intervention in rulemaking process. Currently, OFPP gets involved in acquisition policy problems only when they reach the rulemaking stage. By then, considerable damage has been done. The current process for issuing changes to the FAR and agency FAR supplements is slow and cumbersome and does not afford the private sector a meaningful opportunity to weigh in. As you know, a FAR case is typically opened in either the Defense Acquisition Regulations Council or the Civilian Agency Acquisition Council. Once the initiating council has finished drafting a rule—a process that can take months—it is sent to the other council for action, followed by a process to reconcile the differences between the two versions, which likewise can take months. All council deliberations are shrouded in secrecy. By the time a rule is issued for public comment in the *Federal Register*, the statutory deadline is fast approaching—or, in some cases—has already passed, and an interim rule allowing for comment is often the preferred route.

Then, industry has 60 days in which to weigh in, which is not a very long time, especially when a number of proposed or interim rules are issued at about the same time, which often happens. When the issue is controversial or has far-reaching consequences, the agency may hold a public meeting and/or issues an advance notice of proposed rulemaking and/or a second proposed rule after it has analyzed the public comments, further delaying the process and needlessly expending scarce agency resources.

We submit that industry be given an opportunity to get involved sooner in the rulemaking process, before issuance of an advance/proposed/interim rule. One option is to revise the Federal Advisory Committee Act (FACA) to require the councils to hold public meetings on pending regulatory initiatives on a quarterly basis. Such meetings would serve as a forum that would allow industry representatives to make known their concerns with respect to particular matters. In this way the government would have greater awareness early on that something is amiss as well as better insight into possible alternative regulatory or policy avenues to pursue. After all, the purpose of FACA is not to limit industry access to government but only to ensure that that access is not manipulated to exclude legitimate interested parties.

By involving industry upfront, concerns could be vetted before the government has expended considerable time and effort drafting a rule. In addition to better informing

the rulemaking process, early involvement on the part of industry would expedite the process.

Another option is to devise an early warning mechanism within OFPP. Currently, there is no procedure for handling acquisition policy issues *before* they become crises. Contractors are reluctant to bring problems to the attention of their government customers for fear of being labeled as not team players, and so must use trade and professional associations as intermediaries. The indirect route can be time-consuming and frustrating. The better, and earlier, the communication, the greater the likelihood that issues like cascading set-asides and subcontractor labor under T&M contracts can be resolved before they get out of hand.

10. Institutionalized approach to lessons learned. To help upgrade the sophistication of the government buyer of commercial and performance-based services, we recommend that you consider the establishment of a Lessons Learned office under the Defense Acquisition University that would analyze and document what worked and what didn't work on procurements, with particular emphasis on troubled programs. This shouldn't be seen as an audit function or an effort to pin blame on individuals. Rather, it should be a an opportunity for professionals from the defense and civilian agency acquisition workforce to take a hard look at procurement programs and review case studies of procurements to assess how the reality of contract performance compared to the promise of the proposal. This sort of analytical exercise would go a long way to ensuring that success stories are memorialized as best practices and mistakes are avoided. This body of knowledge also should be made available to procurement officials to better inform policy development and help shape future procurements. We have a lessons learned program within SAIC that looks at our wins and loses in the competitive market and find it to be a very valuable undertaking and a good way to avoid repeating mistakes.

Conclusion. In conclusion, we urge the Section 1423 Panel to address the issues concerning the procurement of services by the government with a view toward recognizing the commercial business environment in which such procurement takes place. We believe that restoring greater consistency and predictability to the acquisition of services, minimizing nonvalue-added requirements, putting in place mechanisms to nip problems in the bud, and, lastly, recognizing the inherent limitations of any system and working within realistic parameters, will ultimately work to the government customer's benefit by better enabling the government to acquire a wide array of services efficiently and effectively and in a timely manner.

This concludes my prepared remarks.

I would be pleased to answer any questions you might have.

Attachment 7

NORTHROP GRUMMAN

DEFINING THE FUTURE

Service Contracting

Acquisition Advisory Panel
Long Beach, CA

27 July 2005

John H. Young
Vice President, Corporate Contracts & Pricing
Northrop Grumman Corporation

Agenda

- **Northrop Grumman Today**
- **Service Contracting:**
  - Positive Experiences
  - Areas for Improvement
- **Q & A Session**

Northrop Grumman Today

- **One of world's leading defense companies**
- **$30B sales in 2004**
  - $7B in service contracts to the Government
- **$60B total backlog**
- **125,000 people, 50 states, 25 countries**
- **Leading capabilities in:**
  - Systems integration
  - C4ISR and battle management
  - Information technology and networks
  - Defense electronics
  - Naval shipbuilding
  - Space and missile defense

Service Contracting- Positive Experiences

- **Increased opportunities to offer services not traditionally provided**
  - Gives government more flexibility in a changing environment
  - Results in better, faster and less costly services through standardization of best practices
  - Allows for use of limited Government / Military personnel in more critical roles
- **Increased awareness and recognition of the benefits of the Safety Act in Federal procurements**

Outsourcing of services has benefited both the Government and Industry

Service Contracting- Positive Experiences (continued)

- **Use of multiple award pre-negotiated GSA agreements, GWACs*, and other agency agreements increasing and have:**
  - Provided for streamlined procurement processes
  - Significantly reduced the cost of doing business for Government and Industry
- **Rapid Response (CECOM) and the Seaport E (Navy) contracts have dramatically reduced cycle time for source selections**
  - Contracts historically awarded in 6-12 months are now awarded in a few weeks / months

Streamlined contracting practices similar to industry trend have made it faster and cheaper to procure services

*Government-Wide Acquisition Contract

Service Contracting- Areas for Improvement

- Allow the marketplace to dictate what bidders receive as a reasonable profit on all allowable costs

- Allow contractors to apply overhead burdens to all elements of cost in accordance with their government approved overheads

Competitive profits encourage more companies to bid, which keeps prices in check

Service Contracting- Areas for Improvement (continued)

- **Simplify the definition of commercial services**
  - Mirror definition applied to commercial products
  - Eliminate the requirement that standalone services be based on established catalog or market prices for specific tasks or outcomes
- **Eliminate non-commercial requirements that increase costs to the Government**
  - Reduce the level of ACRN* validation / reconciliation
  - Eliminate back-up documentation from invoices under Wide Area Workflow (WAWF) electronic billing

Reduced requirements reduces cost

*Accounting Classification Reference Number

Service Contracting- Areas for Improvement (continued)

- **Make statutory changes to permit Time & Material (T&M) and Labor Hour (LH) contracts to be used in sole source situations when price reasonableness is supported**
- **Revise FAR Part 12 to reflect SARA statutory changes granting authority to use T&M and LH contracts to acquire commercial services if award is competitive**
- **Consistently apply Organizational Conflict of Interest (OCI) concepts across and within agencies**
  - Inconsistent application may unintentionally disqualify a services provider from supplying follow-on hardware

Increased use of T&M and LH contracts will bring Government in line with standard commercial practices

Service Contracting- Areas for Improvement (continued)

- **Recognize contractor's need for indemnification in the post 9/11 terrorism environment**
  - Increase application of Safety Act and P.L. 85-804 coverage
- **Improve Safety Act implementation process**
  - Recognize and include guidance regarding Safety Act implementation in the FAR
  - Streamline application and approval process
- **Include Third Party Liability protection for Anti-Terrorism support services**
  - "Insurance – Liability to Third Persons" in all contract types (FAR 52.228.7)
  - "Limitation of Liability Services" (FAR 52.246.25)

Companies must mitigate catastrophic risk in order to provide services to the USG

Conclusion

- Significant improvements have been made over the past few years
- Further opportunities for improvements in cycle time and cost reductions exist for Service Contracting
- Implementing these improvements remains our collective challenge

Q&A Session

Public Meeting
Acquisition Advisory Panel
July 27, 2005
Hyatt Regency Long Beach
Prepared Statement of Richard Hollis
Chief Executive Officer and Founder of Hollis-Eden Pharmaceuticals
Before the Acquisition Advisory Panel

Chairwoman Madsen, members of the panel, thank you for this opportunity to appear before you today.

The federal government spends more than $320 billion on products and services each year. As a market actor the federal government purchases everything from soup to nuts—literally—along with consulting services, advanced communications technologies, and futuristic weapons systems.

Today, however, I want to talk about a relatively small, yet highly innovative component of that marketplace: the $5.6 billion, multi-year BioShield program. While this program may be relatively small in size compared with the cost of a new fleet of aircraft carriers or wing of stealth bombers, this program may be the most important step we can take in better securing the United States against a terrorist attack using weapons of mass destruction (WMD).

I. Overview of the BioShield Program—A Groundbreaking Concept

The theory behind BioShield is elegant in its simplicity: If we can find cures to counter the weapons of mass destruction a terrorist may use against us, the ability of a terrorist to do great harm to our nation is significantly diminished. Every weapon of mass destruction—nuclear, biological, chemical and radiological—we can counter is an arrow taken out of the terrorists quiver.

This capability is particularly important in this era of asymmetrical threats where terrorists don't leave return addresses and where small, non-state actors with no military to speak of can inflict immense harm if they have access to the right weapons. Radiation from a nuclear or dirty bomb penetrates the best armor. You can't outgun a microbe. We need medical counter-measures to these threats.

Consider the example of Hollis-Eden and the nuclear threat.

Recently, the head of the Domestic Nuclear Detection Office at the Department of Homeland Security, Vayl Oxford, stated, "I tell my people, assume there is a 100 percent chance someone will try to attack us with a nuclear weapon in the next five to ten years." Similar conclusions have been reached by a number of recent prominent analyses of the threat of a nuclear or radiological attack, including those by Harvard professor Graham

Allison, the Monterrey Institute, and the Nuclear Threat Initiative, headed by former Senator Sam Nunn.

Contrary to popular belief, the majority of the victims of a nuclear attack would die not from the blast, but from Acute Radiation Syndrome (ARS). They will die over the next two weeks from Acute Radiation Syndrome or ARS. ARS kills by damaging the bone marrow; victims are killed by white blood cell loss and opportunistic infection or bleeding out from platelet loss. The British Medical Journal recently estimated that a 12.5 kiloton bomb detonated in New York City would kill at least 50,000 people instantly. But another 200,000 would be expected to die later from ARS and sicken an additional 700,000 more from the affects of ARS.

Imagine if you could treat ARS with a low cost, self-administered, non-toxic, stable drug that had no side effects. You could literally save hundreds of thousands of lives. You could protect first responders who could then be sent in to conduct rescue and relief efforts. You could substantially decrease the burden on a health care system that will be overwhelmed. And, most importantly, you could dramatically reduce the incentive—the level of terror—that drives terrorists like Osama bin Laden to seek to use nuclear weapons.

In fact, we can. Hollis-Eden is developing a drug called HE2100 or NEUMUNE. This drug works by boosting the body's own innate immune system. To date, results of test in over 200 non-human primates treated with NEUMUNE demonstrated the drug to be safe and effective in the treatment of ARS. In one recent trial, 90 percent of the treated primates survived otherwise lethal doses of radiation, while only 55 percent of the untreated group survived. Extrapolating these results using the numbers of people who will be exposed to ARS in a nuclear attack on a major American city shows the dramatic effect this drug could have in reducing the number of casualties in such an event.

There is no other drug available now or in the development pipeline that can treat ARS.

However, in practice, developing such a counter-measure is no small task. It takes over ten years and hundreds of millions of dollars to develop a new drug. In our case, Hollis-Eden has spent and continues to spend tens of millions of dollars to fund expensive trials and other development costs conducted by AFRRI and elsewhere. In fact, we have spent over $100 million to develop NEUMUNE, and we are on the verge of spending millions more for the required manufacturing scale up process, pivotal efficacy and safety trials for the drug to qualify for approval, which we anticipate filing for in 2006

Only one-in-ten drugs that enter the Food and Drug Administration (FDA) approval process are ever approved. At the same time, the operating margin for successful biopharma companies is 2.76 to 3.74 times the operating margins for major defense contractors. In other words, the opportunity cost for a biotechnology company considering pursuing a medical counter-measure is extremely high. And, most pharmaceutical companies—and as importantly their investors—are reluctant to pursue a

market that has only one likely customer, particularly where that customer is the federal government.

A recent report by the American Venture Capital Association, a consortium of the private investors who fund emerging biotech companies, determined that the pharmaceutical industry hasn't invested in biodefense because the market has only one customer (the federal government), offers lower than average profit margins, is fraught with political vulnerability, and is plagued by uncertain liability and patent protection. Fittingly, this report is entitled, "Government Market Enigma Causes Industry to Stick with What They Know."

Against this backdrop, most pharmaceutical companies have continued to invest their time and resources to finding new cures for cancer, premature baldness, erectile dysfunction and more obviously lucrative efforts.

However, it is important to underscore that industry isn't the problem here—in fact, as I will discuss later, it is the solution. Most pharmaceutical companies are publicly traded. Those of us who run these companies have a fiduciary duty to our investors to maximize shareholder value. As the Michigan Supreme Court said in the seminal case *Dodge v. Ford Motor Company* a "business corporation is organized and carried on primarily for the profit of stockholders" and that "[t] he powers of the directors are to be employed for that end." This understanding is vital to developing a fully effective BioShield program.

At the same time, the federal government has no expertise in drug development. Various federal agencies, such as the National Institutes of Health, fund and conduct outstanding basic research. However, while basic research can produce knowledge that may identify ideas for new drugs, such research is a far cry from the business of actually developing a drug, taking it through pre-clinical and clinical trials, and then through the rigorous Food and Drug Administration approval process. Moreover, given the costs of drug development—hundreds of millions of dollars in sunk costs—the federal government's present day biodefense budget cannot afford to pursue the vast numbers of promising medical counter-measures to the multitude of threats our nation faces today—to say nothing of the dangers of new bioengineered threats we may face tomorrow.

Put simply, this nation needs a biodefense capability and for that effort to be effective it must foster an engaged, focused private sector biodefense industry.

Recognizing this, in 2004, the President and Congress enacted BioShield. BioShield was intended to provide the private sector with a series of market-based incentives to encourage the pharmaceutical industry to focus on developing new medical counter-measures.

The bill as described by Dr. Mark McClellan, then-FDA Commissioner, at the 2003 BIOCEO conference was very straightforward and simple to understand for interested companies and investors. He described the process as one in which the secretaries of HHS and DHS would collaborate and agree on the major chemical, biological,

radiological and nuclear (CBRN) threats and unmet medical needs to those threats. Once the threats were established, the secretary of HHS and his department would then assess what type of medical countermeasures were needed to address that threat. During the scientific assessment of new technology if the scientific experts thought it was feasible to develop such a countermeasure within eight years, the federal government would enter into an advanced purchase contract with that company committing the federal government to buy the product upon successful FDA approval. Dr. McClellan went on to emphasize that BioShield advance purchase contracts must be of a size and scope—"hundreds of millions of dollars"—in order to encourage the industry to participate and to justify their investment in biodefense product development.

The statutory framework described by Dr. McClellan is based on three groundbreaking changes to how the federal government purchases medical counter-measures. And, I would argue more broadly that these changes offer a model for how to encourage more innovative and entrepreneurial behavior in government procurement writ large.

Defining the market: Under the statute the Department of Homeland Security (DHS), in conjunction with the Department of Health and Human Services (HHS), was charged with identifying the series of threats for which the federal government was seeking to purchase medical counter-measures. This process is known as the "Material Threat Assessment" or "MTA." In economic terms DHS was charged with defining the market: we need X million treatments for threat A, Y million for threat B, and so on.

Providing early market incentives and shifting risk: Under the BioShield law, HHS was then authorized to enter into early stage advance purchase contracts with companies that presented something more tangible than a good idea as to how to address one of the priority threats. Under the terms of these contracts, the company would only get paid if they produced a drug that was capable of being stockpiled and ultimately FDA approved. In other words, HHS would not be responsible for funding the development of these drugs, nor would the agency be out anything if the prospective drug failed to work. These protections are critical in an industry where only one-in-ten drugs receive FDA approval.

On the other hand, by offering at an early stage binding terms, such contracts were intended to allow the company to go to the private sector to obtain the capital necessary to develop its promising drug. As Dr. McClellan said the size of these contracts would be such that they would provide companies with ROI sufficient to justify investing in this space to their shareholders and other investors. Investors, aware of the specific market and the potential return on investment if the company was successful in developing the drug, would do their due diligence and based on their analysis decide to invest or not. Companies that were seen as having the ability to deliver would be able to raise more than sufficient private capital to fund drug development without having to wade through a slow and bureaucratic taxpayer funded grant process.

Under this paradigm envisioned by the BioShield Act, government would be able to shift the heavy risk of drug development from the taxpayer to the informed investor and the

pharmaceutical companies. If a drug failed the taxpayer would have lost nothing and the burden of risk and return is on the investor.

It would also allow HHS the ability to leverage the relatively small amount of funding it was provided for BioShield. The Tufts Center for the Study of Drug Development estimates that industry expends more than $800 million on average to develop a new chemical entity. With initially only $5.6 billion in guaranteed markets for BioShield products, BioShield monies need to leverage private investment if the program is to work. (By way of comparison, the federal budget for missile defense—for a system designed to thwart a Cold War era threat, not today's threats—is just under $7 billion per year).

BioShield as proposed and signed by the President and enacted by Congress is a groundbreaking, market-based, highly innovative, entrepreneurial-focused, federal procurement program.

II. Implementation Issues Undercut BioShield's Ability to Succeed and Serve as an Entrepreneurial, Market-Based Procurement Program

However, the program has not been implemented in a manner consistent with that vision.

First, the markets remain undefined: During a recent hearing on BioShield before the Before the House Subcommittee on Emergency Preparedness, Science and Technology of the Committee on Homeland Security, Michael Greenberger, Professor of Law and Director of the University of Maryland Center for Health and Homeland Security testified that:

> The [BioShield] Act established no procedure for DHS to employ in supervising the making of the material threat determinations. Despite what was an obvious Congressional invitation to summarily determine what are the widely recognized [WMD] threats to the United States, DHS has employed an opaque, highly bureaucratized, relatively lengthy process for determining material threats. Over the course of the past year, this cumbersome and poorly delineated administrative process has led to only four material threat determinations. Findings have been made that Anthrax, Smallpox, Botulinum toxin and radiological/nuclear devices pose a material threat to the United States. DHS officials have promised that by the close of this fiscal year material threat determinations will be made concerning plague, tularemia, and viral hemorrhagic fevers . . . . DHS's lassitude in supervising the making of material threat findings is mystifying. The legislative history of the statute is replete with references to a myriad of agents, beyond the four agents identified, posing a substantial threat to the United States.

The American Venture Capital Association, a consortium of the investors who fund early-stage biotech companies, recently issued a report entitled "Government Market Enigma Causes Industry to Stick with What They Know." This investors' report concluded that biodefense is not an open market and the field is "politically charged with shifting priorities." This is not the sort of defined market environment that will attract industry involvement.

Second, HHS hasn't incorporated "the market" into their thinking: Capital markets react to everything and they do so in very real time. These markets are based on expectations—expectations of performance and timing being the two most important factors. Some may argue that on occasion these expectations are unrealistic, however, that isn't the point. Whether reasonable or unreasonable, in order for BioShield to be effective, it needs to harness the markets, not work against them. In order to do so, HHS has to understand how the markets act and react. To date it has not.

The experience of my company provides a concrete example of how this has undercut efforts to develop new drugs to protect the American people from terrorist threats.

Two weeks after the devastating September 11, 2001 attacks on our country, officials from the Armed Forces Radiobiology Research Institute ("AFRRI"), a research division of the Department of Defense, approached Hollis-Eden and informed us that they wanted to fast track the development of one of our experimental drugs for the treatment of ARS.

Given that our product is the single available treatment for the single greatest threat our nation faces, one would assume that HHS has moved with all possible speed to procure this drug. However, four years after 9-11 and AFRRI's entreaty to us, and a year after the passage of BioShield and at this time we do not have a contract. In fact, there isn't even a final RFP out for a nuclear medical counter-measure.

DHS has provided HHS with the required MTA. In October of 2004, HHS put out a request for information to assist the agency in procuring a drug for ARS. Our information leads us to believe that we will be the only fully qualifying bidder. As a result of the information provided under the RFI, HHS is well aware of what interest there is in this procurement and what potential therapies may be offered to it under a RFP. As a result, it would be entirely appropriate for HHS to make use of the authorities under Project BioShield, or even the typical-FAR authorities, to award a contract to Hollis-Eden as quickly as possible. While there are other products that purport to treat ARS, they are in very early stage of development, only beginning the regulatory process for licensure. Moreover, they are being produced by more or less "virtual" companies that have spent less than $300,000 in the development of their purported treatments based upon public filings. Thus, the very idea that HHS will conduct a competition for a product it knows has no comparable equivalent simply does not make sense. However, HHS has not moved to issue the RFP, let alone move to a sole source contract.

On May 20 of this year, the Department of Health and Human Services issued a Special Notice, advising of its intent to issue a Draft Request for Proposals by the end of July 2005 to acquire a drug for the prevention and/or treatment of Acute Radiation Syndrome.

At a recent hearing of the House Government Reform Committee on BioShield implementation, Chairman Davis derisively likened this additional Draft RFP interim step to the high school-esque relationship of "being engaged to be engaged."

Long delays, such as the one we have faced, are now routine in BioShield procurement efforts and they have sent the markets the wrong signal. The investor community sees these delays and reads into them that the federal government is simply not serious about procuring drugs for WMD threats and, generally speaking, developing a BioShield industry.

Again allow me to use Hollis-Eden experiences to illustrate this point. Since 9-11 our company has focused on the development of a drug to address the greatest threat to this nation. At the outset this brought enormous amounts of positive attention on the company. The investor community felt certain that the federal government would leap at the chance to protect the American people from a nuclear attack—it seemed a "no brainer." Recall, immediately after 9-11 the Department of Defense came to us asking us to develop this drug for homeland security. Our stock rose on this positive attention.

Over the course of the next three years we have made extraordinary scientific strides in developing our drug. First, we demonstrated 100 percent survival rates in mice after lethal doses of radiation. Then, we demonstrated up to 90 percent survival rates in primates after lethal doses of radiation—the first drug ever to show an ARS survival benefit. Our IND with FDA was recently approved to initiate human safety studies in the U.S.. In short, we have consistently achieved the major milestones required of the company. If we had shown similar progress in treating any number of other diseases—cancer or heart disease, for example—our stock would be soaring.

However, because the investor community thought procurement of a nuclear medical counter-measure was a "no brainer," HHS' delays and other mixed messages caused uncertainty. This, coupled with the general lack of confidence in biodefense, has caused Hollis-Eden to lose more than $600 in market cap.

And, we are not alone. BioShield was intended to stimulate the biodefense sector. However, since BioShield's passage—with limited exceptions—every company that is active in this sector has seen their share price drop.

Aethlon Medical is developing viral filtration devices that rapidly reduce the presence of infectious disease and toxins in the body that was used in the wake of the anthrax attacks. In March of 2004, in anticipation of BioShield, Aethlon's stock was trading in the $2.75 range. Delays in passing BioShield drove the share price down. At the time of BioShield's passage Aethlon's stock was trading around $1.02. Since BioShield's passage their share price has steadily eroded. Aethlon is now trading in the $.225 range.

MDM Group is developing WMD vaccines and screening products. Like Aethlon, its shares peaked in early 2004 on BioShield anticipation. At the time its stock price broke the $4 mark. By the time of BioShield's passage the stock was in the $2.65 range. It is now trading in the $1.22 range.

Avant Immunotherapeutics is developing biodefense vaccines. In early 2004 its shares traded at just under $4.00. By the time of BioShield's passage its shares were trading around $1.39. Now its stock is trading in the $1.35 range.

Acambis is developing vaccines for infectious diseases such as West Nile and typhoid. The company is currently under contract by the National Institutes of Health to develop a new smallpox vaccine. It shares also peaked in early 2004 around $60. The company then split its stock. As would be expected, their share price dropped, and then rose, but then it began to decline again. By the time BioShield passed, Acambis' shares were trading in the $13.30 range. Today the stock is trading around $8.25.

Clearly there is a disturbing pattern here. And, this is to say nothing of the scores of smaller biotech companies that are trying to break into this market with exciting products but cannot obtain investor money because the market is reticent to back BioShield companies without defined markets, clear timelines, and known not unknown risks.

Put bluntly, the program is having exactly the opposite effect of what was intended. This is particularly sad as BioShield has enormous promise to both safeguard our nation and revolutionize government procurement to a more entrepreneurial, market-based approach.

Third, HHS has failed to utilize the market incentives that are at the heart of the program: To date HHS has only extended a form of advance purchase contract in only one instance: the purchase of a next generation anthrax drug. Instead, according to testimony given by Senator Joseph Lieberman, HHS will not even consider extending a contract for a BioShield drug until the FDA has granted an IND. Senator Lieberman further testified that:

> This interpretation makes no sense and may substantially inhibit the effectiveness of BioShield. The concept behind BioShield is that the government will provide detailed specifications regarding the market for a medical countermeasure so companies can assess whether to risk their capital to develop the countermeasure. This concept applies to research and procurement of any medicine, including those that are long-term research projects that might take many years to reach the IND stage.

Senator Lieberman was one of the two main proponents and primary drafters of the BioShield statute. His view that the IND trigger is not in keeping with the legislative intent should carry great weight.

Moreover, an IND starting line is particularly inappropriate given the nature of the WMD drug development and approval processes. Unlike most drugs, WMD drugs cannot be tested on humans. Instead, WMD drugs are reviewed under the "Animal Efficacy Rule." Under this rule, a WMD drug must show efficacy in nonhuman primates, safety in humans, and similar biochemical responses to the drug in humans and nonhuman primates. As a result, by the time an IND is filed for a WMD drug, the drug is, in most instances, at or near the very end of its development and approval processes—almost all the risks inherent in developing the drug have been taken, and almost all the investments required to fund development have been made. In other words, HHS is intervening so late in the process that its procurement decisions are not encouraging investment in the companies developing BioShield drugs or in the sector as a whole. Rather than driving the market, HHS is riding the market—and this added weight risks breaking the back of the biodefense industry.

BioShield was designed to provide early market signals to encourage the private sector to invest in—and bear the risks of—developing new drugs for WMD threats. However, BioShield increasingly seems to be reverting back to a more traditional government-funded research and development program, one in which HHS selects specific grant recipients to fund experimental development efforts. The risk of a government grant model is two-fold: First, only one-in-ten potential drugs ever receive FDA approval and make it to market. If HHS utilizes Project BioShield to focus on drug development and not procurement, as might appear to be the case thus far, the odds are against picking drugs that will ultimately make it into the Strategic National Stockpile. Second, if HHS picks winners and losers at the early development stage, the industry as a whole will not expend its potentially vast sums of private R&D capital to develop these products for the federal government. Instead, this will become a niche market made up of just a few NIH/HHS companies dependent on federal research grants. As a result, the breadth of technology, knowledge and discovery that will be focused on safeguarding this nation will be only a fraction of what a broader, private sector-based program would provide.

Fourth, HHS has not created an effective, transparent partnership with industry: While I know there are sometimes national security concerns that must be borne in mind when publicly discussing these issues, the fact of the matter is that it has been extraordinarily difficult, if not impossible, to find out anything about this process or about how we, as a small biotech company, might contribute to it. It truly has been very much a "black box" process, and one that we have had to hire several outside consultants to even begin to understand. HHS should now publicly indicate the threats for which it intends to buy products, along with reasonable information about the potential size of the order, the requirements for the products, and approximately when the order will occur. And then HHS should affirmatively open a dialogue with the pharmaceutical and biotechnology industries and with individual companies. This is as obvious as it is true, without better communication with industry, Project BioShield will very simply fail.

III. Putting BioShield Back on Track

Luckily, the program as a whole is conceptually sound. For Project BioShield to be effective and stimulate private companies and investors to participate it simply needs to be implemented the way the law was written.

DHS and HHS have to swiftly define the threats for which the government is seeking to purchase medical counter-measures. To achieve this, the MTA process needs to be dramatically streamlined. By defining these threats, the government will help define the markets for companies and investors. This will allow companies to know what the government wants, when it wants it, and how much of it will be needed.

In reality, however, an MTA isn't a market, it is the promise of a market. In BioShield and other federal procurement efforts there is no market until the lone customer steps up to the plate. Hollis-Eden knows this better than most. As a result, HHS has to then significantly speed the release of RFP's for these drugs. Having witnessed BioShield's problems to date, the markets are not ready to respond on just a MTA for a threat; the markets are waiting to see RFP's—the promise of true contracts.

HHS also must be more open with companies that approach it with innovative treatments for these threats where RFP's may not be issued or where the particular drug does not easily fit an issued RFP. If HHS is only willing to look at one specific way to address one specific threat, one at a time, we may never get past the first threat or two. It can take years to find a treatment for a specific disease. We still don't have a cure for the common cold—and not for a lack of trying. In a perfect world there would be scores of open RFP's—corresponding to the multitude of serious threats we face—on the street waiting for companies that think they have a solution.

HHS should also be much quicker to issue RFP's to promising technologies—at times even issuing multiple RFP's on a single threat and creating a competition among companies. Remember, using the BioShield procurement process doesn't cost the taxpayer anything until a company delivers a safe and effective treatment for a weapon of mass destruction.

In addition, if HHS wants to engage the pharmaceutical industry as a whole in BioShield-related research and drug development, the contracts issued under the program need to be of sufficient size and provide adequate returns on investment to allow these companies to justify BioShield investments to their investors. As then-FDA Commissioner Dr. McClellan emphasized in 2003, BioShield advance purchase contracts must be of a size and scope—"hundreds of millions of dollars"—in order to encourage the industry to participate and to justify their investment in biodefense product development.

IV. Conclusion

The United States has the most innovative, persistent and effective pharmaceutical industry by far of any country in the world, and we have only begun to unleash that

amazing potential for the protection of the American people from acts of terrorism. It is difficult to navigate and steer at the same time. And, in the case of BioShield, the government, industry and the investor community are literally drawing the map, while trying to determine a course, at the same time we all have a hand on the ship's wheel trying to steer. As a result the program has yet to achieve its full promise. However, with a few mid-term course corrections the full potential of BioShield can be realized.